

1984

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### Recommended Citation

Louis M. Solomon and Robert D. Joffe, *Exclusive Distribution and Antitrust*, 53 Fordham L. Rev. 491 (1984).

Available at: <https://ir.lawnet.fordham.edu/flr/vol53/iss3/4>

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## Exclusive Distribution and Antitrust

### Cover Page Footnote

The authors wish to thank Robin C. Landis for his comments on an earlier draft of this article.

# EXCLUSIVE DISTRIBUTION AND ANTITRUST

LOUIS M. SOLOMON\*

AND

ROBERT D. JOFFE\*\*

## INTRODUCTION

EXCLUSIVE distribution exists when a supplier utilizes only one outlet for the sale of his wares in a particular geographic area.<sup>1</sup> Although most commonly employed by manufacturers of goods requiring point-of-sale services,<sup>2</sup> exclusive distributorships are adaptable to most business settings.<sup>3</sup>

The creation, maintenance, termination, or transfer from one distributor to another of an exclusive distributorship may preclude rival or potential distributors from dealing in the supplier's product. The actual or perceived loss of business resulting from that preclusion has prompted claims of antitrust violations by excluded parties, the Department of Justice, and the Federal Trade Commission. Although such claims have been asserted ever since the Sherman Act was enacted,<sup>4</sup> to this day courts and commentators have accorded exclusive distribution inconsistent

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The authors wish to thank Robin C. Landis for his comments on an earlier draft of this Article.

1. See, e.g., L. Sullivan, Handbook of the Law of Antitrust § 147, at 423-24 (1977); Note, *Restricted Channels of Distribution Under the Sherman Act*, 75 Harv. L. Rev. 795, 824-27 (1962) [hereinafter cited as *Distribution Under the Sherman Act*]. Exclusive distribution agreements have also been called exclusive franchise, exclusive selling, sole outlet, exclusive dealership, and exclusive agency arrangements. See L. Sullivan, *supra*, at 424. We use the terms "distributor" or "dealer" generically to refer to distributors, retailers, or other firms in the chain of distribution between manufacturer or supplier and ultimate consumer.

2. See *Distribution Under the Sherman Act*, *supra* note 1, at 795.

3. See *infra* notes 159-208 and accompanying text.

4. See *infra* notes 44-47 and accompanying text. Section 1 of the Sherman Act declares illegal "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States," and § 2 makes it unlawful to "monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States." Ch. 647, §§ 1-2, 26 Stat. 209, 209 (1890) (codified as amended at 15 U.S.C. §§ 1-2 (1982)).

Although § 1 is most frequently used to challenge exclusive distributorships and hence is of primary interest here, litigants also invoke § 2. See, e.g., *Smith v. Northern Mich. Hosps., Inc.*, 703 F.2d 942 (6th Cir. 1983); *Woolen v. Surtran Taxicabs, Inc.*, 461 F. Supp. 1025 (N.D. Tex. 1978). Discerning the anticompetitive potential of exclusive franchising, a fundamental inquiry in the § 1 context, is also critical to the § 2 analysis by virtue of the case law equating acts of monopolization with anticompetitive conduct. E.g., *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 275 (2d Cir. 1979), *cert. denied*, 444 U.S. 1093 (1980); *Telex Corp. v. IBM*, 510 F.2d 894, 925 (10th Cir.), *cert.*

treatment.<sup>5</sup> Some commentators, for example, argue that exclusive franchises "create significant territorial barriers to competition" and embody "territorial restraint[s] most threatening to competition."<sup>6</sup> Others urge that exclusive franchising should be treated like other nonprice "vertical"<sup>7</sup> restraints and tested under the principles laid down by the Supreme Court in *Continental T.V., Inc. v. GTE Sylvania Inc.*<sup>8</sup> Still others claim that exclusive distribution should be treated as presumptively lawful "in the absence of monopoly."<sup>9</sup> Others simply state that it is legal "in the absence of monopolistic purpose or anticompetitive effect."<sup>10</sup>

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dismissed, 423 U.S. 802 (1975); see *Northeastern Tel. Co. v. AT & T*, 651 F.2d 76, 93 (2d Cir. 1981), cert. denied, 455 U.S. 943 (1982).

5. See *MLC, Inc. v. North Am. Philips Corp.*, 1983-1 Trade Cas. (CCH) ¶ 65,351, at 70,097 (S.D.N.Y. May 3, 1983) ("Exclusive [representation] arrangements have been a source of mischief in the antitrust laws for a considerable period of time."); L. Sullivan, *supra* note 1, at 424 ("Dilemmas abound about the way the law should respond to exclusive dealerships.").

6. Louis, *Vertical Distributional Restraints Under Schwinn and Sylvania: An Argument for the Continued Use of a Partial Per Se Approach*, 75 Mich. L. Rev. 275, 282, 286 (1976) [hereinafter cited as Louis I]. Louis argues that the reason courts occasionally condone "unreasonable and unlawful" exclusive franchising arrangements is because of a "bright-line trade off" "whereby some restraints are conclusively unreasonable and others [including exclusive franchising] are presumptively reasonable in order to avoid the hard question of reasonableness in most cases." *Id.* at 287; see Louis, *Vertical Distribution Restraints After Sylvania: A Postscript and Comment*, 76 Mich. L. Rev. 265, 273 & nn.47-48 (1977).

7. We employ the common usage of "vertical": "when a firm operating at one level of an industry places restraints upon rivalry at another level." R. Bork, *The Antitrust Paradox* 288 (1978). This definition excludes restraints that are vertical in form only but are actually imposed by horizontal cartels at any level in the chain of distribution (for example, territorial allocations that are compelled not by the manufacturer but by colluding retailers). We also exclude arrangements whose purpose and effect are to eliminate competition by substitutes for the manufacturer's product. See *id.* at 229-30; F. Scherer, *Industrial Market Structure and Economic Performance* 300-05 (2d ed. 1980).

8. 433 U.S. 36 (1977). See Baker, *Interconnected Problems of Doctrine and Economics in the Section One Labyrinth: Is Sylvania a Way Out?*, 67 Va. L. Rev. 1457, 1515-20 (1981); Elias, *Dealer Termination or Exclusion, Intrabrand Competition and GTE Sylvania*, 29 Baylor L. Rev. 435 *passim* (1977).

9. Malina, *The Antitrust Jurisprudence of the Second Circuit*, 37 Rec. A.B. City N.Y. 436, 457 (1982); accord, e.g., Greenberg, *Unilateral Refusals to Deal*, 42 Antitrust L.J. 305, 307 (1973); Handler & Lazaroff, *Restraint of Trade and the Restatement (Second) of Contracts*, 57 N.Y.U. L. Rev. 669, 710-11 (1982); Steuer, *Non-Price Vertical Sales Restraints*, Fourth Ann. Seminar on Distrib. 1, 12 (1982).

10. Zelek, Stern & Dunfee, *A Rule of Reason Decision Model After Sylvania*, 68 Calif. L. Rev. 13, 17 n.29 (1980); see Handler & Lazaroff, *supra* note 9, at 711 ("it cannot be gainsaid that exclusive representation agreements may offend restraint of trade principles"). Although stating that exclusive distributorships "are usually, although not invariably, upheld," Judge Posner's most recent article on restricted distribution expressly excludes discussion of exclusive franchising. See Posner, *The Next Step in the Antitrust Treatment of Restricted Distribution: Per Se Legality*, 48 U. Chi. L. Rev. 6, 7 (1981) [hereinafter cited as Posner I].

We note that on January 23, 1985, the Department of Justice issued Vertical Restraints Guidelines. See U.S. Dep't of Justice, *Guidelines for Vertical Restraints*, reprinted in Trade Reg. Rep. (CCH) No. 687 Pt. II (Jan. 30, 1985) [hereinafter cited as Vertical Guidelines]. The guidelines' treatment of exclusive distribution is unclear. *Com-*

This Article considers the antitrust treatment of exclusive distribution.<sup>11</sup> Its thesis is that such arrangements cannot harm competition, can be procompetitive, and should be treated as lawful by antitrust enforcement agencies and courts. Part I briefly contrasts exclusive distribution with two other vertical arrangements that bear the label "exclusive." After Part II addresses the economics of exclusive franchising, Part III places judicial treatment of exclusive distribution in historical context. Part IV explores whether there are any distinctions between exclusive franchising and other vertical arrangements that justify treating the for-

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*pare id.* at 12-13 (discussing the legality of manufacturer's appointing one or more distributors and his "mere refusal to sell through other outlets") with *id.* at 19-20 (treating exclusive distribution agreements like exclusive dealing contracts and allowing that exclusive distributorships could result in anticompetitive foreclosure).

11. We treat herein exclusive franchising in and of itself and do not specifically address the legality of transferring an exclusive franchise from one distributor to another. Many courts analyze the legality of franchising by examining the competitive effect, if any, of transferring the franchise or of substituting one franchisee for another and not by examining the propriety of granting the franchise in the first place. *See, e.g.,* Car Carriers, Inc. v. Ford Motor Co., 1984-2 Trade Cas. (CCH) ¶ 66,220, at 66,910 (7th Cir. Oct. 2, 1984); Walker v. U-Haul Co., 734 F.2d 1068, 1071-72 (5th Cir. 1984); Dun & Mavis, Inc. v. Nu-Car Driveaway, Inc., 691 F.2d 241, 245 (6th Cir. 1982); Carlson Mach. Tools, Inc. v. American Tool, Inc., 678 F.2d 1253, 1259-60 (5th Cir. 1982); Chandler Supply Co. v. GAF Corp., 650 F.2d 983, 989 (9th Cir. 1980); Aladdin Oil Co. v. Texaco, Inc., 603 F.2d 1107, 1116-17 (5th Cir. 1979); Golden Gate Acceptance Corp. v. GMC, 597 F.2d 676, 678 (9th Cir. 1979); Dreibus v. Wilson, 529 F.2d 170, 173 (9th Cir. 1975); Burdett Sound, Inc. v. Altec Corp., 515 F.2d 1245, 1248-49 (5th Cir. 1975); Ark Dental Supply Co. v. Cavitron Corp., 461 F.2d 1093, 1094 (3d Cir. 1972); Joseph E. Seagram & Sons, Inc. v. Hawaiian Oke & Liquors, Ltd., 416 F.2d 71, 81-82 (9th Cir. 1969), *cert. denied*, 396 U.S. 1062 (1970); Ace Beer Distributors, Inc. v. Kohn, Inc., 318 F.2d 283, 286-87 (6th Cir.), *cert. denied*, 375 U.S. 922 (1963); Westbury Donuts, Inc. v. Dunkin' Donuts of Am., Inc., 1982-2 Trade Cas. (CCH) ¶ 64,951, at 72,887 (E.D.N.Y. July 12, 1982); Westpoint Pepperell, Inc. v. Rea, 1980-2 Trade Cas. (CCH) ¶ 63,341, at 75,744 (N.D. Cal. April 8, 1980). For cases analyzing the question whether dealer substitution, or the mere "shifting" of business from one dealer to another, would have sufficient effect on interstate commerce to invoke the federal court's jurisdiction under the Sherman Act, compare *Englert v. City of McKeesport*, 736 F.2d 96, 98-99 (3d Cir. 1984) (rejecting the argument that mere "shifting" does not have the requisite impact on interstate commerce) and *Cardio-Medical Assocs. v. Crozer-Chester Medical Center*, 721 F.2d 68, 71-75 (3d Cir. 1983) (same) and *James R. Snyder Co. v. Associated Gen. Contractors*, 677 F.2d 1111, 1114-15 (6th Cir.) (to satisfy the jurisdiction requirement, plaintiff need only allege an interrelationship between the intrastate activity that was the target of the anticompetitive conduct and a specific aspect of interstate commerce), *cert. denied*, 459 U.S. 1015 (1982) with *Moles v. Morton F. Plant Hosp., Inc.*, 1980-81 Trade Cas. (CCH) ¶ 63,600, at 77,188-89 (M.D. Fla. May 10, 1978) (alleged effect on interstate commerce found insufficient to invoke Sherman Act jurisdiction), *aff'd mem.*, 617 F.2d 293 (5th Cir.), *cert. denied*, 449 U.S. 919 (1980). *Cf. Furlong v. Long Island College Hosp.*, 710 F.2d 922, 927 (2d Cir. 1983) ("[I]t is not easy to imagine how the exclusion of Dr. Furlong from [the hospital] might be shown to have a predictable tendency to restrict the defendants' purchase of supplies from out of state."); *Harron v. United Hosp. Center, Inc.*, 522 F.2d 1133, 1134 (4th Cir. 1975) (dismissing "for want of a substantial federal question and a consequent lack of jurisdiction"), *cert. denied*, 424 U.S. 916 (1976).

We also do not separately discuss issues relating solely to the termination of a franchise—for example, whether there existed the concert of action required under § 1. *See Spray-Rite Serv. Corp. v. Monsanto Co.*, 684 F.2d 1226, 1234 (7th Cir. 1982), *aff'd*, 104 S. Ct. 1464 (1984).

mer more leniently than the latter. Finally, Part V addresses how one might utilize the legal and economic principles of exclusive distribution theory in examining the competitive consequences of various business arrangements, including the appointment of exclusive agents to run transportation facilities, sports stadiums, or other "essential facilities," the appointment of exclusive providers of services at hospitals, and the inclusion in shopping center leases of exclusive tenancy clauses.

### I. NOMENCLATURE

Courts and commentators use the term "exclusive" to describe at least three different types of vertical arrangements. First, exclusive distribution or franchising, the form of exclusivity considered in this Article, results when a manufacturer agrees with his sole distributor not to appoint additional distributors in the area serviced by the contracting distributor.<sup>12</sup> The effect of such an agreement is to limit the freedom of the manufacturer, who cannot thereafter appoint or sell through another distributor in the area granted to the first distributor.<sup>13</sup> The exclusive distribution agreement might also prohibit the manufacturer from distributing his own goods in the area serviced by the exclusive franchisee. The exclusive franchisee remains free to deal in the goods of other suppliers, including competitors of the first manufacturer, and may sell to any customer.

An exclusive franchise may but need not completely shelter the exclusive distributor from the selling efforts of the manufacturer's other distributors. When, for example, the manufacturer appoints exclusive distributors in a number of different geographic areas, and when transportation costs do not preclude the shipment of goods from one area to another, rivalry can exist among distributors of the manufacturer's product.<sup>14</sup> It is fair to suppose, however, that if the manufacturer desired

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12. See *supra* note 1. A distributorship can be de facto exclusive without an express agreement between manufacturer and distributor. A manufacturer can simply appoint a distributor in a particular geographic area and refrain from appointing any other. Such unilateral action and inaction would not violate § 1. *E.g.*, *United States v. Colgate & Co.*, 250 U.S. 300, 307 (1919); *Fuchs Sugars & Syrups, Inc. v. Amstar Corp.*, 602 F.2d 1025, 1030 (2d Cir.), *cert. denied*, 444 U.S. 917 (1979); see Zelek, Stern, & Dunfee, *supra* note 9, at 17 n.29. For the purposes of this Article, we assume the existence of an agreement sufficient for § 1 purposes.

13. It is common to speak of the limitation on the manufacturer's freedom to deal as a "restraint" or a "restriction." Baker, *supra* note 8, at 1515. Of course, the distribution agreement likely places many different restraints on both manufacturer and distributor. The restraints forming the sorts of exclusive distribution arrangements discussed herein arise as a result of negotiation and in the absence of physical coercion.

14. [E]xclusive dealerships, unlike territorial or location restrictions on dealers, cannot be used to stamp out intrabrand competition entirely. If the authorized dealer sets prices too high, or provides inadequate service, promotes inefficiently or otherwise creates market opportunities, a dealer authorized and receiving shipments elsewhere can ship goods into the exclusive area and sell them there.

L. Sullivan, *supra* note 1, at 424. Of course, Sullivan's analysis assumes the appointment of more than one exclusive distributor.

maximum rivalry among his distributors he would not voluntarily have granted any exclusive distributorships.

A second type of arrangement denominated "exclusive" exists when the distributor promises a supplier to refrain from handling the goods of competing suppliers.<sup>15</sup> Usually called "exclusive dealing," this arrangement restricts the distributor, who contracts away the freedom to market the goods of manufacturers competing with the contracting manufacturer.<sup>16</sup> As a theoretical matter, exclusive franchising might be said to foreclose competitors of the distributor from dealing in the goods of the contracting manufacturer in the same manner that exclusive dealing might be said to foreclose competitors of the contracting supplier from distributing through the particular distributor. Legal commentary, however, has generally used foreclosure terminology to describe the anticompetitive potential of only dealer-restraining, exclusive dealing arrangements.<sup>17</sup>

Finally, a manufacturer and distributor can agree that the distributor will sell the manufacturer's product only within a specified territory. This arrangement, often referred to as creating an "exclusive sales territory," limits the distributor's, not the manufacturer's, freedom to deal, and the freedom circumscribed is the distributor's ability to sell the goods of the

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15. See generally *FTC v. Brown Shoe Co.*, 384 U.S. 316 (1966) (decided under § 5 of the Federal Trade Commission Act); R. Bork, *supra* note 7, at 299-309 (discussing exclusive dealing and requirements contracts); Marvel, *Exclusive Dealing*, 25 J.L. & Econ. 1 (1982) (same); Steuer, *Exclusive Dealing in Distribution*, 69 Cornell L. Rev. 101 (1983) (same).

16. A related form of agreement is the requirements contract, whereby the seller agrees to supply all of the buyer's requirements for a specified product for a certain duration. See, e.g., *Tampa Elec. Co. v. Nashville Coal Co.*, 365 U.S. 320, 322 (1961); *Standard Oil Co. v. United States*, 337 U.S. 293, 296 (1949).

17. See Baker, *Vertical Restraints in Times of Change: From White to Schwin to Where?*, 44 Antitrust L.J. 537, 541 (1975).

Without justifying the difference in approach, we note that the foreclosure of distributors wishing to market the products of a particular manufacturer may neither as frequently nor as clearly affect the delivery of goods or services to the ultimate consumer as might the "foreclosure" of discrete manufacturers. Although it is difficult to quantify how much buyer (*i.e.*, distributor) concentration exists in the United States, an "impressionistic view suggests that concentration on the buyers' side is generally more modest than concentration on the sellers' side." F. Scherer, *supra* note 7, at 297. "Buyer concentration in [the] vast consumer goods market is obviously low." *Id.* We note further that specific legislation exists only with respect to exclusive dealing — *i.e.*, potential manufacturer foreclosure. See 15 U.S.C. § 14 (1982) (Section 3 of the Clayton Act, ch. 323, § 3, 38 Stat. 731 (1914)) (making it unlawful to "lease or make a sale or contract for sale of goods . . . on the condition, agreement or understanding that the lessee or purchaser thereof shall not use or deal in the goods . . . of a competitor or competitors of the lessor or seller").

The distinction between manufacturers and distributors blurs somewhat as the latter begin to provide more services or assume a greater role in the delivery of the final product to the consumer. That consideration may explain, though again not justify, why some courts and the enforcement agencies appear to analyze exclusivity arrangements for the provision of hospital services under the exclusive dealing rubric. See *infra* notes 190-204 and accompanying text.

contracting manufacturer in nondesignated territories.<sup>18</sup> The distributor remains free to sell the goods of other manufacturers.<sup>19</sup>

## II. THE ECONOMICS OF EXCLUSIVE DISTRIBUTION

In granting an exclusive franchise, the manufacturer typically shields the franchisee from rivalry by the manufacturer himself and by other distributors of the manufacturer's product.<sup>20</sup> That diminution in rivalry, however, does not of itself diminish the competition faced by the manufacturer.<sup>21</sup> A manufacturer facing stiff competition in the sale of his product to the ultimate consumer prior to the establishment of an exclusive franchise would face the same stiff competition afterwards. Because an exclusive distributorship does not diminish any "interbrand" rivalry,<sup>22</sup> it does not provide the manufacturer with any additional market power.<sup>23</sup> The exclusive franchise would not therefore permit the manufacturer to restrict output or increase price to any greater extent than the

18. See Posner, *supra* note 10, at 6 ("the assignment of exclusive sales territories . . . forbid[s] the distributor or dealer to sell outside of a specified territory on pain of having its relationship with the manufacturer terminated or, perhaps, of having to pay a 'profit passover' or some other charge to the distributor or dealer whose territory it invaded").

19. Of course, various marketing devices can be used in combination with other restrictions on the manufacturer or dealer. Other forms of "restricted distribution" involved in some of the cases discussed herein include location restrictions, pursuant to which the distributor agrees to sell the manufacturer's products from only designated locations, and customer restrictions, which limit the customers to whom the distributor may sell.

20. R. Bork, *supra* note 7, at 289-91; Bork, *The Rule of Reason and the Per Se Concept: Price Fixing and Market Division [II]*, 75 Yale L.J. 373, 397-405 (1966) [hereinafter cited as Bork I]; see 3 P. Areeda & D. Turner, *Antitrust Law* ¶ 734a (1978).

21. 3 P. Areeda & D. Turner, *supra* note 20, ¶ 734d; see R. Bork, *supra* note 7, at 289-91.

22. The Supreme Court in *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977), defined "interbrand competition" and "intra-brand competition" as follows:

Interbrand competition is the competition among the manufacturers of the same generic product . . . and is the primary concern of antitrust law. The extreme example of a deficiency of interbrand competition is monopoly, where there is only one manufacturer. In contrast, intra-brand competition is the competition between the distributors—wholesale or retail—of the product of a particular manufacturer.

*Id.* at 52 n.19.

23. "The term 'market power' refers to the ability of a firm . . . to raise price above the competitive level without losing so many sales so rapidly that the price increase is unprofitable and must be rescinded." Landes & Posner, *Market Power in Antitrust Cases*, 94 Harv. L. Rev. 937, 937 (1981); see, e.g., *National Collegiate Athletic Ass'n v. Board of Regents*, 104 S. Ct. 2948, 2965 n.38 (1984) ("Market power is the ability to raise prices above those that would be charged in a competitive market."); *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 104 S. Ct. 1551, 1566 n.16 (1984) (same); see also *United States v. E. I. duPont de Nemours & Co.*, 351 U.S. 377, 391 (1956) ("Monopoly power is the power to control prices or exclude competition."). A firm with market power can restrict the output of its product, a result that is commonly accomplished by raising the price of the product. See R. Bork, *supra* note 7, at 98-101. For ease of discussion, we will take the hardest case as paradigmatic and assume throughout that the firm exercising market power is a monopolist.



manufacturer could accomplish in the absence of the exclusivity arrangement.<sup>24</sup> Accordingly, from an economic perspective, the antitrust laws should be indifferent to the manufacturer's grant of an exclusive distributorship.<sup>25</sup>

One might argue against that conclusion as follows: Because an exclusive franchise can eliminate rivalry among distributors in the sale of the manufacturer's product, the arrangement has the potential of permitting the franchisee himself to exercise some market power. Were the franchisee capable of exercising market power, he could restrict output of the manufacturer's goods and attempt to reap excess, "monopoly" profits in reselling those goods. Such a restriction would be inefficient and potentially harmful to consumers. If the restriction were made possible by virtue of the exclusivity of the franchise, would not the exclusive franchise clearly be an agreement in restraint of trade?<sup>26</sup>

As support for a general condemnation of exclusive franchising, that argument is unavailing, for it fails to recognize the conditions that must exist before an exclusive franchisee could hope to earn excess profits by restricting output of the manufacturer's goods. Even as a limited proposition justifying challenges to specific instances of exclusive distribution, the argument is unsound; it ignores the theoretical and practical considerations militating against a rational manufacturer's permitting his exclusive franchisee to earn monopoly rents.

In order for an exclusive franchisee to be capable of exercising market power that he does not already have, the exclusive franchise must either eliminate intrabrand rivalry or so greatly diminish it that the franchisee could raise his price without losing a significant number of sales to other franchisees. The existence of franchisees (if any) operating in other territories could circumscribe the exclusive franchisee's ability to raise prices.<sup>27</sup> In addition, the manufacturer would himself have to have market power; easily substituted brands or products would prevent any restriction of output or price rise by the exclusive franchisee.<sup>28</sup> It follows, therefore, that the only instance in which the grant of an exclusive franchise could enable the franchisee to restrict output and price monop-

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24. See R. Bork, *supra* note 7, at 229; Bork, *Vertical Integration and the Sherman Act: The Legal History of an Economic Misconception*, 22 U. Chi. L. Rev. 157, 172 n.65, 196 & n.128 (1954) [hereinafter cited as Bork II]. See *supra* notes 20-21 and accompanying text.

25. Cf. Bork, *Vertical Restraints: Schwinn Overruled*, 1977 Sup. Ct. Rev. 171, 180 & n.20 (addressing other vertical restraints) [hereinafter cited as Bork III]; Posner I, *supra* note 10, at 22-26 (same); Posner, *The Rule of Reason and the Economic Approach: Reflections on the Sylvania Decision*, 45 U. Chi. L. Rev. 1, 13-16 (1977) (same).

26. White, *Vertical Restraints in Antitrust Law: A Coherent Model*, 26 Antitrust Bull. 327, 322-33 (1981); see R. Bork, *supra* note 7, at 230 n., 290; Bork I, *supra* note 20, at 401-02; Meehan & Lerner, *A Proposed Rule of Reason for Vertical Restraints on Competition*, 26 Antitrust Bull. 195, 215 & n.40 (1981).

27. See Landes and Posner, *supra* note 23, at 963-72.

28. See *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 52 n.19 (1977).

olistically is the case in which a manufacturer with market power grants an "airtight" exclusive franchise.

Once it is assumed that the manufacturer has market power, however, the sensible conclusion is that the manufacturer would exercise that power himself, without or prior to instituting exclusive franchising. The manufacturer could exercise market power by, for example, restricting the output of his product or setting his price to the franchisee at a level that reaped whatever excess profits were available.<sup>29</sup> After the manufacturer achieved the profit-maximizing price/output combination in his sales to the franchisee,<sup>30</sup> it would not be in the manufacturer's interest to restrict output further, and no rational manufacturer would do so. The manufacturer need not permit his exclusive franchisee to do so either. One method by which the manufacturer could prevent the franchisee from exploiting the market power potentially available to him by virtue of the exclusivity of the franchise is for the manufacturer to set the maximum price at which the franchisee could resell the product. Although that option is currently unlawful,<sup>31</sup> other, equally effective mechanisms are available. For example, the manufacturer could lawfully impose minimum output requirements on the franchisee,<sup>32</sup> which would have the same effect as setting the maximum resale price.<sup>33</sup> Control sufficient to prevent the exclusive distributor from pricing monopolistically or re-

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29. See 3 P. Areeda & D. Turner, *supra* note 20, ¶¶ 725b, 725c; Posner, *Antitrust Policy and the Supreme Court: An Analysis of the Restricted Distribution, Horizontal Merger and Potential Competition Decisions*, 75 Colum. L. Rev. 282, 283-85 (1975) [hereinafter cited as Posner II].

30. See 3 P. Areeda & D. Turner, *supra* note 20, ¶ 725b ("Under any given cost and demand conditions, there is but one maximum monopoly profit to be gained from the sale of an end-product."); accord R. Bork, *supra* note 7, at 229 ("[A] monopolist has no incentive to gain a second monopoly that is vertically related to the first, because there is no additional monopoly profit to be taken.").

31. *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373, 405 (1911); *Spray-Rite Serv. Corp. v. Monsanto Co.*, 684 F.2d 1226, 1234 (7th Cir. 1982), *aff'd*, 104 S. Ct. 1464 (1984).

Note that although the manufacturer may not lawfully engage in maximum resale price maintenance, it may generally advertise suggested retail prices directly to the public or mark the product with the suggested retail price prior to sale to distributors. See Panel Discussion, *Dos and Don'ts of Distribution*, 53 Antitrust L.J. 363, 374-75 & nn.18-22 (1984) (citing cases).

32. See ABA Antitrust Section, Monograph No. 9, Refusals to Deal and Exclusive Distributorships 2 n.5 (1983); see also *American Motors Sales Corp. v. Peters*, 317 S.E.2d 351, 357 (N.C. 1984) ("The manufacturers retain a tremendous incentive to police pricing abuses by their retailers. They may guard against such practices by establishing and enforcing sales quotas . . .") (citing Smith, *Franchise Regulation: An Economic Analysis of State Restrictions on Automobile Distribution*, 25 J.L. & Econ. 125, 128-29 (1982)).

33. See *supra* note 23. It is true that the ease with which a manufacturer can impose minimum output requirements is in part a function of the observability and complexity of the distributor's resale efforts. But the manufacturer should be able to determine the price/output combination that will prevent the exclusive distributor from reaping supra-normal profits. Furthermore, even if the manufacturer cannot do so himself, he can rely on information provided by other potential distributors (who are vying to become the exclusive distributor), or he can engage in trial and error in setting the minimum level of acceptable output.

stricting output would also exist when the manufacturer is able to force the exclusive distributor to act like a competitive distributor—for example, when there is competition to become the exclusive distributor<sup>34</sup> or when the manufacturer has the power to replace the distributor<sup>35</sup> or to distribute the product himself.<sup>36</sup> Because the manufacturer can effectively control the distributor's level of output, the manufacturer need not fear that the distributor, having been granted an exclusive franchise, will further restrict output or otherwise exercise market power in reselling the manufacturer's goods.

It does not follow that merely because a rational manufacturer need not permit an exclusive franchisee to reap excess profits, the manufacturer will never permit the franchisee to increase gross distribution margins in reselling the products he purchases from the manufacturer. For example, a manufacturer may permit higher margins in order to give the franchisee additional revenue to invest in demand-generating activities such as point-of-sale services. The critical point is that a manufacturer wishes, consistent with maximum effectiveness in selling the end-product, to minimize the cost of distributing his goods.<sup>37</sup> That is true whether or not, incident to enhancing their value, the franchisee raises the price of the goods before reselling them. Should the exclusive distributor mark up the manufacturer's goods to prices reflecting more than minimum costs of distribution but not utilize the additional revenue to make the manu-

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34. The reality of competition "for," as opposed to competition "in," the market has powerful explanatory force. So long as there is competition for the market, consumers are well served. For discussions or applications of the principle of competition for the market, see *Omega Satellite Prods. Co. v. City of Indianapolis*, 694 F.2d 119, 127 (7th Cir. 1982) (citing *United States v. El Paso Natural Gas Co.*, 376 U.S. 651 (1964)); *Parmelee Transp. Co. v. Keeshin*, 292 F.2d 794, 803-04 (7th Cir.), cert. denied, 368 U.S. 944 (1961); *In re Burnham Hosp.*, [1979-83 Transfer Binder] Trade Reg. Rep. (CCH) ¶ 22,005, at 22,580 (Feb. 24, 1983) (FTC Advisory Opinion); R. Posner, *Antitrust Law: An Economic Perspective* 124 & n.60 (1976); Posner II, *supra* note 29, at 285.

35. The threat of termination and appointment of a different franchisee would serve to check anticompetitive schemes of a distributor.

[T]hrough his ability to award the local franchise to some other retailer, the manufacturer should be able to keep retailer margins at competitive levels. In effect, he can periodically auction off the franchise to the retailer who promises the best local market development while minimizing retail margins.

White, *supra* note 26, at 333; see *id.* at 333 n.10.

36. Such vertical integration would be lawful. See cases cited *infra* note 48. See also *Jack Walters & Sons Corp. v. Morton Bldgs., Inc.*, 1984 Trade Cas. (CCH) ¶ 66,080, at 66,025 (7th Cir. June 22, 1984) ("the option of vertical integration places competitive pressure on the firm's suppliers and buyers, who know that if they charge too much for their services the firm may decide to perform them itself").

37. See, e.g., *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 56 & n.24 (1977) (citing Bork I, *supra* note 20 at 403; Posner II, *supra* note 29 at 283, 287-88); 3 P. Areeda & D. Turner, *supra* note 20, ¶ 734d; 88 Harv. L. Rev. 636, 641 (1975); Cf. *Carriers, Inc. v. Ford Motor Co.*, 1984 Trade Cas. (CCH) ¶ 66,220, at 66,910 (7th Cir. Oct. 2, 1984) (action challenging the transfer of an exclusive distributorship on the ground that manufacturer had conspired to permit the new dealer to charge noncompetitive prices; grant of motion to dismiss affirmed, the court of appeals unwilling to believe that the manufacturer "conspired to injure itself").

facturer's product more valuable, not only would consumers be worse off; because the distributor would sell relatively fewer of the manufacturer's goods, the manufacturer would be worse off as well. His revenues and profits will be lower because the output restriction resulting from the franchisee's price rise would not be offset by the enhanced value and higher price of the products that are sold.

Consumers and the manufacturer share the desire to maximize the efficient distribution of the manufacturer's product. When a manufacturer grants an exclusive franchise, therefore, we must assume that the manufacturer's purpose is not to limit rivalry in itself or to permit a distributor to exercise market power but rather to render more efficient the distribution of his product.<sup>38</sup> The manufacturer would not grant the exclusive franchise unless he believed it would make the distribution of his product more efficient.<sup>39</sup>

Three conclusions that will be of assistance below can be drawn from the discussion thus far. First, from an economic perspective, the benign

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38. The precise form of the efficiency may vary from product to product and from industry to industry. See, e.g., *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 55 (1977) (discussing the elimination of the free-rider problem); R. Bork, *supra* note 7, at 430-34 (identifying efficiencies resulting from vertical restraints); R. Posner, *supra* note 34, at 147-51 (identifying economic rationales for manufacturers' restricting competition in the distribution of their goods); Meehan & Larner, *supra* note 26, at 200-12 (discussing, in addition, the minimization of transaction costs).

39. The literature raises two general objections to the efficiency rationale suggested in the text, neither of which we find persuasive. First, some commentators purport to identify a variety of ills with which distributional restraints might be associated. These include the facilitation of other anticompetitive, unlawful behavior (such as cartelization either among manufacturers or distributors); the facilitation of price discrimination; the promotion of inefficient product differentiation; the erection of barriers to entry (foreclosure); and the facilitation of output restriction. See, e.g., Comanor, *Vertical Territorial and Customer Restrictions: White Motor and Its Aftermath*, 81 Harv. L. Rev. 1419, 1422-27 (1968); Meehan & Larner, *supra* note 26, at 212-23; Pitofsky, *The Sylvania Case: Antitrust Analysis of Non-Price Vertical Restrictions*, 78 Colum. L. Rev. 1, 13-14 (1978). See generally R. Bork, *supra* note 7, at 291-98 (discussing various objections to the legality of vertical restraints); Bork I, *supra* note 20, at 405-29 (same). For present purposes, it is sufficient to note that exclusive distribution agreements simply could not facilitate a number of the potential ills identified. See, e.g., Meehan & Larner, *supra* note 26, at 214 n.36, 215 (cartel among manufacturers of products, for which exclusive dealing is required); *id.* at 214-15 (foreclosure or the raising of entry barriers, because an exclusive distribution agreement does not foreclose other manufacturers). As to the other potential ills, the feared activity is either unlawful in itself (for example, dealer cartels or price discrimination) or has been shown to be competitively benign or beneficial. See R. Bork, *supra* note 7, at 291-98.

The second set of objections to the efficiency rationale advances the proposition that the goal of antitrust embraces something more or other than the maximization of consumer welfare or seeks to imbue the notion of consumer welfare with more than that state of affairs resulting from the most efficient manufacture and distribution of goods. See Pitofsky, *The Political Content of Antitrust*, 127 U. Pa. L. Rev. 1051, 1051 (1979) (arguing that the goals of antitrust should include preventing the concentration of economic power, dispersing market decisionmaking authority, and avoiding the political interference that could result if the economy were "dominated by a few corporate giants"); see also Fox, *The Modernization of Antitrust: A New Equilibrium*, 66 Cornell L. Rev. 1140, 1177-92 (1981) (collecting authorities).

nature of exclusive distribution does not depend on the absence of market power on the part of the manufacturer employing the device.<sup>40</sup> Even a monopolist manufacturer need not use the exclusive franchise to restrict output<sup>41</sup> and need not permit his franchisee to exercise any market power that might be bestowed on him by the exclusive nature of the arrangement. The monopolist manufacturer can and will restrict output, but he will not do so to any greater extent by marketing his goods through an exclusive distributor. What he intends to achieve by the appointment is a more efficient method of distribution, which is in his and the public's interest.

Second, the duration of the franchise is irrelevant to the economic inquiry. Whether the distributorship is terminable at will or is to last in perpetuity, the manufacturer would not diminish rivalry among his distributors unless he believed he were receiving a quid pro quo. To obtain the exclusive franchise, the distributor must offer the manufacturer equivalent value for the life of the contract. That value is what the manufacturer has calculated to be his best option. And that value is what enhances efficiency or flows from the enhancement of efficiency and is thus beneficial to consumers. The duration of the arrangement is simply one of the terms bargained for. The manufacturer might calculate incorrectly or bargain poorly, but "[n]o court is likely to make a more accurate assessment than does a businessman with both superior information and the depth of insight that only self-interest can supply."<sup>42</sup>

Finally, the economic principles articulated above hold irrespective of the relative bargaining strengths of the contracting parties. To be sure, a manufacturer with many potential distributors to choose from or with alternative marketing methods at his disposal may be able to exact more from his exclusive franchisee than a manufacturer who faces only one qualified distributor and who, for some reason, cannot expand internally and has no other viable option. Indeed, the manufacturer facing a monopsonistic distributor may not have any choice but to grant an "exclusive franchise," in which case one may have to look to the distributor's interest in efficiency, rather than the manufacturer's, as having prompted the arrangement. But insofar as the market or competitive effects of such an arrangement differ from those suggested by the analysis above, the differences appear to be a function of the buying power of the dealer, which the grant of exclusivity by the manufacturer neither creates nor strengthens.<sup>43</sup>

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40. See *supra* notes 29-30 and accompanying text.

41. R. Bork, *supra* note 7, at 289-90; Bork III, *supra* note 25, at 187-88; Posner II, *supra* note 29, at 283; see *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 745 (7th Cir. 1982); Posner I, *supra* note 10, at 25-26 & n.75.

42. R. Bork, *supra* note 7, at 290.

43. Discussion of the theory of bilateral monopoly is beyond the scope of this Article. For a discussion of that topic, see Allen, *Vertical Integration and Market Foreclosure: The Case of Cement and Concrete*, 14 J. L. & Econ. 251, 255-58 (1971); Comanor, *Vertical Mergers, Market Powers, and the Antitrust Laws*, 57 Proc. Am. Econ. Ass'n 254, 257

## III. JUDICIAL TREATMENT OF EXCLUSIVE DISTRIBUTION

Decided a year after enactment of the Sherman Act, *Chicago, St. Louis & New Orleans Railroad v. Pullman Southern Car Co.*<sup>44</sup> presented a claim by Pullman seeking to void its contract with the railroad. The contract gave Pullman the right to furnish the railroad's drawing-room and sleeping cars for a term of fifteen years.<sup>45</sup> The contract also provided that the railroad would not "contract with any other party to run the said class of cars on and over said lines of road during the said period of fifteen years."<sup>46</sup> Rejecting Pullman's argument that the contract was void as against public policy and "in general restraint of trade," the Supreme Court ruled:

The defendant [railroad company] was under a duty, arising from the public nature of its employment, to furnish for the use of passengers on its lines such accommodations as were reasonably required by the existing conditions of passenger traffic. Its duty, as a carrier of passengers, was to make suitable provisions for their comfort and safety. Instead of furnishing its own drawing-room and sleeping cars, as it might have done, it employed the plaintiff, whose special business was to provide cars of that character, to supply as many as were necessary to meet the requirements of travel. It thus used the instrumentality of another corporation in order that it might properly discharge its duty to the public. So long as the defendant's lines were supplied with the requisite number of drawing-room and sleeping cars, it was a matter of indifference to the public who owned them. . . . We cannot perceive that such a contract is at all in restraint of trade.<sup>47</sup>

The Supreme Court's ruling suggests two principles for establishing the legality of exclusive franchising. First, the Court reasoned from the presumption that the railroad could have furnished its own drawing-room and sleeping cars without raising any restraint of trade concerns. The proposition that vertical integration by internal expansion is permissible under the antitrust laws is not remarkable.<sup>48</sup> The proposition that

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(1977); Machlup & Taber, *Bilateral Monopoly, Successive Monopoly and Vertical Integration*, 27 *Economica* 101, 110-13 (1960). For discussion of a related concept—the "relational" aspects of the manufacturer/distributor relationship—see Baker, *supra* note 8, at 1490-93.

44. 139 U.S. 79 (1891).

45. *Id.* at 89.

46. *Id.*

47. *Id.* For an earlier explication of the principles stated in *Pullman*, see *Express Cases*, 117 U.S. 1, 24-25 (1886); see also *United States v. Addyston Pipe & Steel Co.*, 85 F. 271, 287 (6th Cir. 1898) (citing cases), *modified as to relief*, 175 U.S. 211 (1899).

48. See *United States v. Columbia Steel Co.*, 334 U.S. 495, 525 (1948) ("[V]ertical integration, as such without more, cannot be held violative of the Sherman Act."); *Jack Walters & Sons Corp. v. Morton Bldgs., Inc.*, 1984 Trade Cas. (CCH) ¶ 66,080, at 66,024-25 (7th Cir. June 22, 1984) ("vertical integration is not an unlawful or even a suspect category under the antitrust laws"); *Litton Sys., Inc. v. AT & T*, 700 F.2d 785, 824 (2d Cir. 1983) ("This court has, of course, emphasized that a monopolist may lawfully take advantage of benefits deriving from . . . integration"), *cert. denied*, 104 S. Ct. 984 (1984); *University Life Ins. Co. v. Unimarc Ltd.*, 699 F.2d 846, 852 (7th Cir. 1983)

because the railroad could have expanded internally it could with impunity enter into a fifteen-year contract to the same effect with an independent entity might well be.<sup>49</sup> The Court would have correctly assumed that the railroad would not choose a method of service that was more costly than necessary. Doing so would increase the railroad's costs without providing it with a compensating increase in revenues. Because the railroad could be trusted to maximize its own profit—and in so doing minimize its own and the public's costs—there was no reason to interfere with the railroad's choice.

The second rationale supporting the Court's ruling derives from the statement that, so long as the service was satisfactory, it was "a matter of indifference to the public"<sup>50</sup> which particular companies provided the service. That perception presages by some eighty years the statement in

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("Vertical integration—the performance within one firm of two or more steps in the chain of production and distribution—does not violate the Sherman Act"); *White v. Hearst Corp.*, 669 F.2d 14, 19 (1st Cir. 1982) ("[T]he change by a newspaper publisher of its system of newspaper distribution from that of independent news dealers to distribution by its own employees, *without more*, does not violate Section 1." (citing *Auburn News Co. v. Providence Journal Co.*, 659 F.2d 273, 278 (1st Cir. 1981), *cert. denied*, 455 U.S. 921 (1982))) (emphasis in original); *see, e.g.*, *Red Diamond Supply, Inc. v. Liquid Carbonic Corp.*, 637 F.2d 1001, 1006-07 (5th Cir.), *cert. denied*, 454 U.S. 827 (1981); *Fuchs Sugars & Syrups, Inc. v. Amstar Corp.*, 602 F.2d 1025, 1033 (2nd Cir.), *cert. denied*, 444 U.S. 917 (1979); *Knutson v. Daily Review, Inc.*, 548 F.2d 795, 805-06 (9th Cir. 1976), *cert. denied*, 433 U.S. 910 (1977); *Bowen v. New York News, Inc.*, 522 F.2d 1242, 1258 (2d Cir. 1975), *cert. denied*, 425 U.S. 936 (1976); *Levitch v. CBS*, 495 F. Supp 649, 668 (S.D.N.Y. 1980), *aff'd per curiam*, 697 F.2d 495, 496 (2d Cir. 1983); *Newberry v. Washington Post Co.*, 438 F. Supp 470, 483-84 (D.D.C. 1977); *see also Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 274, 276 (2d Cir. 1979) (the competitive advantages resulting from vertical integration may not form the basis of a § 2 claim), *cert. denied*, 444 U.S. 1093 (1980); *Ampar Enters. v. Reno Newspapers*, 8 Media L. Rep. (BNA) 1670, 1671 (D. Nev. 1982) (It is "the established law that a newspaper publisher's election to substitute a self-distribution system for distribution by independent contractors is not unlawful and is not predatory or anti-competitive conduct under the Sherman Act.").

Courts and commentators have discussed potential anticompetitive effects of vertical integration. *See, e.g.*, *Byars v. Bluff City News Co.*, 609 F.2d 843, 861 (6th Cir. 1979) (discussing the facilitation of price discrimination, the raising of entry barriers, and the evasion of governmental regulation (citing 3 P. Areeda & D. Turner, *supra* note 20, "¶ 725, 726)). Even assuming that the antitrust laws should be concerned with those effects, exclusive distribution either does not enable or promote them (price discrimination and raising entry barriers) or is unnecessary in order to accomplish them (avoidance of governmental regulation).

49. The Supreme Court's reference to vertical integration might have reflected the belief that the market effects of the various forms of vertical integration, whether accomplished through internal expansion or by contract, were identical and therefore should be treated alike by the courts. Alternatively, even assuming differences in the market impact of the various forms of vertical integration, the Court might have been reluctant, as a matter of sound jurisprudence, to create a nonmarket incentive for internal expansion. *See infra* note 156. The Court's reference to vertical integration by internal expansion would then have been an acknowledgement that prohibiting one form of vertical integration would merely prompt the use of another, less efficient method to achieve the same end.

50. *Chicago, St. L. & N.O. R.R. v. Pullman S. Car Co.*, 139 U.S. 79, 89 (1891).

*Brown Shoe v. United States*<sup>51</sup>—made the cornerstone of antitrust jurisprudence in *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*<sup>52</sup>—that the antitrust laws were enacted for “the protection of competition, not competitors.”<sup>53</sup> It presages as well the equally fundamental (though arguably less firmly established) proposition that, in looking at the impact on competition, consumer welfare is the primary reference point.<sup>54</sup>

In his opinion in *United States v. Addyston Pipe & Steel Co.*,<sup>55</sup> Judge Taft explained the legal principle articulated in *Pullman*:

The railroad company may discharge this duty [of furnishing sleeping-car facilities] itself to the public, and allow no one else to do it, or it may hire someone to do it, and, to secure the necessary investment of capital in the discharge of the duty, may secure to the sleeping-car company the same freedom from competition that it would have itself in discharging the duty.<sup>56</sup>

It is not clear from this statement whether Judge Taft was relying upon what is demonstrated by economic analysis: that the “freedom from competition” experienced by the exclusive agent could not be any greater than that experienced by the railroad itself.<sup>57</sup> What does seem clear is the

51. 370 U.S. 294, 320 (1962).

52. See 429 U.S. 477, 488 (1977).

53. *Brown Shoe*, 370 U.S. at 320 (emphasis in original); see *Brunswick*, 429 U.S. at 488; see also *Copperweld Corp. v. Independence Tube Corp.*, 104 S. Ct. 2731, 2740 n.14 (1984) (quoting *Brunswick*, 429 U.S. at 320). See *infra* note 204 and accompanying text. But see Note, *Unclogging the Bottleneck: A New Essential Facility Doctrine*, 83 Colum. L. Rev. 441, 470-71 (1983) (proposing a standard that appears to resurrect the notion of the primacy of discrete competitors) [hereinafter cited as *Unclogging the Bottleneck*].

54. *E.g.*, *National Collegiate Athletic Ass'n v. Board of Regents*, 104 S. Ct. 2948, 2964 (1984) (“Congress designed the Sherman Act as a ‘consumer welfare prescription.’” (quoting *Reiter v. Sonotone Corp.*, 442 U.S. 330, 343 (1979) (quoting R. Bork, *supra* note 7, at 66))); *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 745 (7th Cir. 1982) (“[C]onsumer welfare . . . is the objective that we are told should guide us in interpreting the Sherman Act.”); *Products Liability Ins. Agency, Inc. v. Crum & Forster Ins. Cos.*, 682 F.2d 660, 663 (7th Cir. 1982) (the antitrust laws “are designed to protect the consumer interest in competition”); *Auburn News Co. v. Providence Journal Co.*, 659 F.2d 273, 278 (1st Cir. 1981) (“[I]t must not be forgotten that it is ultimately consumers whom the antitrust laws are designed to protect.”), *cert. denied*, 455 U.S. 921 (1982); see *Copperweld Corp. v. Independence Tube Corp.*, 104 S. Ct. 2731, 2740 (1984); *Apex Hosiery Co. v. Leader*, 310 U.S. 469, 493 (1940); *Roland Mach. Co. v. Dresser Indus., Inc.*, 1985-1 Trade Cas. (CCH) ¶ 66,329, at 66,544 (7th Cir. Dec. 21, 1984).

55. 85 F. 271 (6th Cir. 1898), *modified as to relief*, 175 U.S. 211 (1899). “Circuit Judge (later Chief Justice) Taft’s opinion for the court in *United States v. Addyston Pipe & Steel Co.*, . . . has generally been recognized—and properly so—as a fully authoritative exposition of antitrust law.” *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 618 (Burger, C.J., dissenting).

56. *Addyston Pipe*, 85 F. at 287.

57. See *supra* notes 21-36 and accompanying text. Professor (now Judge) Bork observed the following about Judge Taft’s opinion:

Taft saw that since the railroad company could furnish the sleeping-car facilities itself without competition, nothing is lost if it grants to its hired sleeping-car company the same freedom from competition. In fact, something must be gained. The railroad company will choose between offering the services itself and getting some other firm to offer them on the basis of comparative cost. The



presence of the two principles identified above: the reasoning from internal expansion and the supremacy of competition and consumer welfare over the protection of discrete competitors.<sup>58</sup>

*Donovan v. Pennsylvania Co.*<sup>59</sup> amplified those two themes. Pennsylvania Company operated a railroad and Union Passenger Station, one of six railway stations in Chicago.<sup>60</sup> Union Station was the only terminus in Chicago for the five railroads that used it.<sup>61</sup> At issue in *Donovan* was the legality of a contract between Pennsylvania Company and Parmelee Transfer Company by which Parmelee alone would furnish Union Station with "all vehicles necessary for the accommodation of passengers arriving there on [Pennsylvania's] trains or on the trains of other railroad companies."<sup>62</sup> The question presented was whether Pennsylvania Company could exclude Donovan and other non-Parmelee hackmen from Union Station.<sup>63</sup>

Noting that Pennsylvania Company held legal title to the property on which the station was situated, the Supreme Court ruled that, so long as the railroad fulfilled its responsibilities to the public, it was "under no obligation to refrain from using its property to the best advantage of the public and of itself. It [was] not bound to so use its property that others, having no business with it, may make profit to themselves."<sup>64</sup> Furthermore, the Court stated, the "railroad company was not bound to accord this particular privilege to the defendants simply because it had accorded a like privilege to the Parmelee Transfer Company."<sup>65</sup>

That exclusive franchising was lawful remained the opinion of the Supreme Court through *United States v. Bausch & Lomb Optical Co.*,<sup>66</sup>

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decisions to bring in a sleeping-car company means a judgment that that is the less costly method. The vertical restraint results in no increase in output restriction but effects some decrease in costs, a net benefit to consumers.

R. Bork, *supra* note 7, at 289.

58. Indeed, Judge Taft arguably goes further, stating that the railroad could, by refusing to deal, shield itself from its competitors. See *infra* note 186 and accompanying text.

59. 199 U.S. 279 (1905).

60. *Id.* at 280-81.

61. *Id.* at 281.

62. *Id.* at 292.

63. *Id.*

64. *Id.* at 294.

65. *Id.* at 296. The Court added:

It is true that by its arrangement with the railroad company the Parmelee Company was given an opportunity to control, to a great extent, the business of carrying passengers from the Union Passenger Station to other railway stations and to hotels or private houses in Chicago. But in a real, substantial, legal sense, that arrangement cannot be regarded as a monopoly in the odious sense of that word, nor does it involve an improper use by the railroad company of its property.

*Id.* at 297.

66. 321 U.S. 707, 719 (1944). Prior to *Bausch & Lomb*, the Court in *Black and White Taxicab & Transfer Co. v. Brown & Yellow Taxicab & Transfer Co.*, 276 U.S. 518 (1928), relied on *Donovan* and rejected the argument that the grant of an exclusive franchise "prevents competition, makes such discrimination as is unreasonable and detrimental to

in which an equally divided Court affirmed a district court ruling<sup>67</sup> that upheld Bausch & Lomb's agreement to sell its entire output of pink-tinted eyeglass lenses through Soft-Lite.<sup>68</sup> At this juncture, however, confusion arose. On the basis of dictum in *Bausch & Lomb*,<sup>69</sup> the Department of Justice took the position that vertical territorial and customer restrictions placed on *distributors*, unlike exclusive distribution agreements that restrain only the manufacturer, were per se unlawful.<sup>70</sup> The Department entered into a number of consent decrees prohibiting such arrangements.<sup>71</sup>

At about that time, two frequently cited lower court opinions, *Packard Motor Car Co. v. Webster Motor Car Co.*<sup>72</sup> and *Schwing Motor Co. v. Hudson Sales Corp.*,<sup>73</sup> upheld exclusive distribution agreements but did so because the automobile manufacturers employing them were small and had experienced a decline in their respective market shares. The courts stated that neither manufacturer "dominate[d] the market in the commodity,"<sup>74</sup> "effective competition exist[ed] at both the seller and buyer levels,"<sup>75</sup> and the restraints were imposed for the purpose of "competing with a large manufacturer."<sup>76</sup> Neither *Packard* nor *Schwing* cited *Pullman*, *Addyston*, or *Donovan*, which had upheld or approved exclusive distribution without examining the market share of the supplier, the effectiveness of competition, or the purpose of employing that form of distribution. Neither lower court opinion explained why those considerations were deemed relevant, and neither identified any anticompetitive potential of exclusive franchising.

Coinciding with the Department's new view of dealer territorial and customer restraints and with the unfortunate reasoning of *Packard* and *Schwing*<sup>77</sup> was the increased use of dealer-confining, exclusive territory

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the public and constitutes such a preference over other transfer men as to give [the exclusive franchisee] a practical monopoly of the business." *Id.* at 526-27. Three years after *Bauch & Lomb*, the Court in *United States v. Yellow Cab Co.*, 332 U.S. 218 (1947), again cited *Donovan* and stated in dictum: "It is true, of course, that exclusive contracts for the transportation service in question are not illegal." *Id.* at 229.

67. *United States v. Bausch & Lomb Optical Co.*, 45 F. Supp. 387 (S.D.N.Y. 1942), *aff'd*, 321 U.S. 707, 719 (1944).

68. *Id.* at 399.

69. 321 U.S. at 721, 724.

70. See Handler, *Reforming the Antitrust Laws*, 82 Colum. L. Rev. 1287, 1298 & nn.67-69 (1982); *Distribution Under the Sherman Act*, *supra* note 1, at 796 & n.6.

71. See Handler, *supra* note 70, at 1298 & nn.67-69; *Distribution Under the Sherman Act*, *supra* note 1, at 797.

72. 243 F.2d 418 (D.C. Cir. 1957).

73. 138 F. Supp. 899, *aff'd mem. per curiam*, 239 F.2d 176 (4th Cir. 1956), *cert. denied*, 355 U.S. 823 (1957).

74. *Schwing*, 138 F. Supp. at 906.

75. *Packard*, 243 F.2d at 420 (quoting Handler, *Annual Antitrust Review*, 11 Rec. A.B. City N.Y. 367, 370 (1956)).

76. *Id.* at 421. As the dissent noted, the restraints were imposed "for the purpose of improving the manufacturer's competitive position vis-a-vis more powerful manufacturers." *Id.* at 421 n.1.

77. It is ironic that *Packard* and *Schwing* have been considered examples of favorable

arrangements.<sup>78</sup> Analyses of exclusive sales territories were combined with discussions of exclusive distribution agreements. For example, one Note defined an "exclusive territorial distributorship" as both "a covenant by the manufacturer . . . that the manufacturer will not sell to anyone else within that same area" and "the setting of a limited area within which a retailer or wholesaler will confine his sales efforts."<sup>79</sup> The confusion arising from lumping together analyses of manufacturer constraints and dealer territorial constraints was exacerbated by the author's statement that the "exclusive territorial distributorship" under examination was "also known as exclusive representation and exclusive agency,"<sup>80</sup> terms more commonly descriptive of exclusive distribution agreements as we have defined them here.<sup>81</sup> The author concluded that the "exclusive territorial distributorship has a large hurdle to overcome before it should be permitted."<sup>82</sup> Yet the Note never differentiated between exclusive distribution and dealer territorial confinement, cited interchangeably dealer restraint cases and exclusive franchise cases in which no dealer restraint existed,<sup>83</sup> and did not address the relevant Supreme Court cases.

Another Note,<sup>84</sup> written after the district court decision but before the Supreme Court decision in *White Motor Co. v. United States*,<sup>85</sup> also did not consider the Supreme Court precedent discussed above. That Note, which has been frequently cited, asserted without supporting citation that "[t]he Department . . . is reported to have expressed the view that exclusive franchise arrangements may also [like dealer-based territorial and customer restraints] be illegal per se . . . ."<sup>86</sup>

Illegal per se! No case to our knowledge had ever so held. Indeed, in *White Motor*,<sup>87</sup> in which the Department of Justice sought to establish

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judicial treatment of exclusive franchising. See Elias, *supra* note 8, at 436 & n.4. In fact, neither case was as thoroughly reasoned or as favorable as the earlier Supreme Court cases. Also noteworthy is the fact that the statements in *Schwing* were probably dicta; after the manufacturer terminated the complaining plaintiff and granted the allegedly "exclusive" distributorship, "there were two other Hudson dealers in the Baltimore metropolitan area." 138 F. Supp. at 902.

78. See Note, *The Resurgence of the Exclusive Territorial Distributorship as an Antitrust Problem*, 40 Minn. L. Rev. 853, 853-55 (1956) [hereinafter cited as *Resurgence*].

79. *Resurgence*, *supra* note 78, at 853.

80. *Id.* at 853 n.1.

81. See *supra* notes 1, 12-19 and accompanying text.

82. *Resurgence*, *supra* note 78, at 862.

83. See *id.* at 855 n.13, 862 & n.52.

84. *Distribution Under the Sherman Act*, *supra* note 1.

85. 372 U.S. 253 (1963). See *infra* notes 87-88 and accompanying text.

86. *Distribution Under the Sherman Act*, *supra* note 1, at 797. The author concluded that the "prior law [did not] appear so compelling, either for or against an approach of per se illegality, as to foreclose further investigation and analysis" of exclusive distribution. *Id.* at 799.

87. *United States v. White Motor Co.*, 194 F. Supp. 562 (N.D. Ohio 1961), *rev'd*, 372 U.S. 253 (1963). White Motor manufactured medium and heavy duty trucks and truck parts. It marketed its goods principally through some 200 "franchised distributors" who in turn sold to some 85 dealers. White also sold directly to governmental units and so-called "National Accounts." *Id.* at 564-65. White's relations with its outlets were stan-

the per se unlawfulness of dealer territorial and customer restraints, the Department did not even challenge the manufacturer's use of exclusive franchises. And the Supreme Court in that case *reversed* the district court's grant of the government's motion for summary judgment,<sup>88</sup> ruling that it knew "too little of the actual impact of both [the territorial] restriction and the one respecting customers to reach a conclusion on the bare bones of the documentary evidence before us."<sup>89</sup>

Four years after *White Motor* came *United States v. Arnold, Schwinn & Co.*,<sup>90</sup> which scrutinized and held unlawful per se certain dealer-based customer and territory restrictions.<sup>91</sup> In dictum, the *Schwinn* Court stated:

[A] manufacturer of a product other and equivalent brands of which are readily available in the market may select his customers, and for this purpose he may 'franchise' certain dealers to whom, alone, he will sell his goods. *Cf. United States v. Colgate & Co.*, 250 U.S. 300 (1919). If the restraint stops at that point—if nothing more is involved than vertical 'confinement' of the manufacturer's own sales of the merchandise to selected dealers, and if competitive products are readily available to others, the restriction, on these facts alone, would not violate the Sherman Act.<sup>92</sup>

A number of courts and commentators rely on the *Schwinn* dictum to support the proposition that exclusive distribution is generally lawful.<sup>93</sup> In context, however, the language is troublesome, adding another layer of confusion to that engendered by *Packard*, *Schwinn*, and the contemporaneous legal commentary. To begin, the passage in *Schwinn* is susceptible to the reading that exclusive franchising is sanctioned because of its unilateral character. The Court's citation to *Colgate*, which upheld manufacturer policing of dealer pricing because the manufacturer acted uni-

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dardized by form contracts, and distributors were required to use forms prepared by White when entering into agreements with dealers. *Id.* at 566. The contracts granted distributors exclusive selling rights within their respective territories. *Id.* For their part, distributors agreed to territorial and customer limitations. *Id.* at 566-67.

88. *White Motor*, 372 U.S. at 264. In granting the government's motion for summary judgment, the district court stated in dictum that exclusive distribution agreements had "been upheld as reasonable when ancillary to the sale of goods for resale because they protect the vendee's property rights in his resale business from being destroyed or damaged by the actions of his vendor who is in a position to undersell, or establish a competitor of, his vendee." 194 F. Supp. at 578.

89. *White Motor*, 372 U.S. at 261. The Supreme Court did not have occasion to discuss exclusive distributorships. In his concurring opinion, Justice Brennan cited *Packard* and *Schwinn* and stated that because of the small size and declining nature of the manufacturers' market shares, those decisions were "of necessarily limited scope." *Id.* at 269 n.8 (Brennan, J., concurring).

90. 388 U.S. 365 (1967).

91. *Id.* at 382.

92. *Id.* at 376.

93. See, e.g., Baker, *supra* note 8, at 1515; Greenberg, *supra* note 9, at 307; Note, *Vertical Agreements to Terminate Competing Distributors*, 92 Harv. L. Rev. 1160, 1165 & n.56 (1979).

laterally,<sup>94</sup> supports such a reading.<sup>95</sup> The line of cases beginning with *Pullman*, however, was not grounded on the manufacturer's right unilaterally to choose his customers but on the principle that no cognizable restraint of trade resulted from even the explicit contractual grant of an exclusive franchise.<sup>96</sup> Equally disturbing is *Schwinn's* reference to "other and equivalent brands" and to "competitive products" being "readily available to others."<sup>97</sup> The Court did not provide a rationale for that requirement, yet it is not obvious why the existence of competing products should act as a legal constraint on the manner in which a manufacturer may market his own goods. The manufacturer's endeavor to minimize distribution margins is all the "constraint" required, for, as noted above, "[w]hen the manufacturer chooses, he chooses on criteria that also control consumer welfare."<sup>98</sup> The "others" to whom the *Schwinn* Court referred are other distributors, but the earlier cases had expressly refused to protect the interests of discrete participants in the competitive process at the expense of competition and consumer welfare.<sup>99</sup>

The last Supreme Court case meriting discussion is *Continental T.V., Inc. v. GTE Sylvania Inc.*<sup>100</sup> The restrictions in *Sylvania* took two forms: limiting the number of franchises granted for any given area and requiring each distributor to sell Sylvania televisions from only those locations at which he was franchised.<sup>101</sup> The franchised dealers remained free to sell competing brands of televisions, and Sylvania remained free to cancel the franchise or to appoint additional franchisees in any area.<sup>102</sup> Acknowledging that "[n]o dealer was given an exclusive dealership for a particular area,"<sup>103</sup> the court of appeals in *Sylvania* ruled that *Schwinn's* per se rule was inapplicable in part because of the "exclusive dealership precedents."<sup>104</sup> The court stated:

In an exclusive dealership arrangement a manufacturer agrees with a dealer not to authorize any competing dealers to sell the manufacturer's products anywhere within the exclusive territory of the first dealer. There is a veritable avalanche of precedent to the effect that, absent sufficient evidence of monopolization, a manufacturer may legally grant such an exclusive franchise, even if this effects the elimination of another distributor.<sup>105</sup>

Determining that *Schwinn* did not control, the court of appeals stated that it feared the "grievous implications for the common and established

94. *United States v. Colgate & Co.*, 250 U.S. 300, 306-08 (1919). See *supra* note 12.

95. See *supra* text accompanying note 92.

96. See *supra* notes 44-66 and accompanying text.

97. *Schwinn*, 388 U.S. at 376.

98. R. Bork, *supra* note 7, at 290.

99. See *supra* notes 51-54, 56-58, 64 and accompanying text.

100. 433 U.S. 36 (1977).

101. 433 U.S. at 38.

102. *Id.*

103. *GTE Sylvania Inc. v. Continental T.V., Inc.*, 537 F.2d 980, 983 (9th Cir. 1976), *aff'd*, 433 U.S. 36 (1977).

104. *Id.* at 997.

105. *Id.*

practices of franchising and the granting of exclusive dealerships" if the territorial restrictions at issue were declared unlawful *per se*.<sup>106</sup>

The Supreme Court affirmed the conclusion reached by the court of appeals but could not reconcile *Schwinn*. Like the court of appeals, the Supreme Court observed that a Sylvania franchise did not constitute an airtight exclusive distributorship: Sylvania retained the freedom to increase the number of dealers in an area if, in its view, the existing dealers were not adequately developing the area.<sup>107</sup> The Court noted further that in both *Schwinn* and in the case before it "the restrictions limited the freedom of the retailer to dispose of the purchased products as he desired."<sup>108</sup> Although the particular forms of vertical restraint at issue in *Schwinn* differed in some respects from those employed by Sylvania,<sup>109</sup> the Supreme Court deemed the differences irrelevant from a "functional antitrust analysis"<sup>110</sup> and refused to treat them differently. The Court overruled *Schwinn* and instated a rule of reason standard for examining the vertical restraints before it.<sup>111</sup> That standard was left undelineated by the Supreme Court but was to have something to do with ascertaining the interbrand and possibly the intrabrand effects of the challenged restraint.<sup>112</sup> The Court also stated that "departure from the rule-of-reason standard must be based upon demonstrable economic effect rather than—as in *Schwinn*—upon formalistic line drawing."<sup>113</sup> The Supreme Court did not refer to the "veritable avalanche" ("absent sufficient evidence of monopolization")<sup>114</sup> of exclusive franchise precedent relied on by the court of appeals or, indeed, to the exclusive distribution line of cases at all.

Although *Sylvania* relaxed the standard for testing nonprice vertical restraints,<sup>115</sup> the change wrought by that case to the law of exclusive franchising is as unclear as was the law itself after *Packard*, *Schwinn*, and the *Schwinn* dictum. Some cases continue "to rely on the exclusive deal-

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106. *Id.* at 998. The court of appeals grounded the feared "grievous implications" on the fact that if exclusive distribution were permitted while the restraints at issue in *Sylvania* were deemed illegal *per se*, then once "*a dealer is franchised anywhere he is franchised everywhere.*" *Id.* (emphasis in original).

107. *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 38 (1977).

108. *Id.* at 46.

109. *See id.* The *Sylvania* Court noted that the restraints imposed by Sylvania and *Schwinn* reduced but did not eliminate "competition among their respective retailers." *Id.* As noted above, exclusive distributorships do have the potential for eliminating such "competition." *See supra* note 14.

110. *Sylvania*, 433 U.S. at 46.

111. *Id.* at 58-59.

112. *See id.* at 56, 57 n.27. *See infra* notes 133-40 and accompanying text.

113. 433 U.S. at 58-59.

114. *GTE Sylvania Inc. v. Continental T.V., Inc.*, 537 F.2d 980, 997 (1976), *aff'd*, 433 U.S. 36 (1977).

115. *But cf. Sylvania*, 433 U.S. at 58 (the Court stating that, in holding as it did, it did "not foreclose the possibility that particular applications of vertical restrictions might justify *per se* prohibition under *Northern Pac. R. Co.*").

ership precedents even after the *Sylvania* decision."<sup>116</sup> Others test exclusive distributorships under the interbrand/intrabrand rubric suggested by *Sylvania*.<sup>117</sup> Other decisions are more circumspect. In *Woolen v. Surtran Taxicabs, Inc.*,<sup>118</sup> for example, the plaintiff cab drivers challenged under section 1 the grant to another concern, after competitive bidding, of the exclusive right to pick up passengers at the Dallas/Fort Worth Airport.<sup>119</sup> The district court acknowledged *Donovan* but stated that it was unclear "[w]hy this exclusive contract should enjoy a virtual judicial exception from antitrust scrutiny."<sup>120</sup> In addition to "[u]nreasoned obedience" to Supreme Court precedent,<sup>121</sup> the court offered and rejected two possible explanations.<sup>122</sup> According to the court, the failure to subject exclusive distribution to the same sort of "antitrust inspection"<sup>123</sup> as other vertical restraints resulted from judicial "fiat [and has] led to untoward distinctions."<sup>124</sup> The court denied the defendant's motion to dismiss the complaint.<sup>125</sup> Other recent cases have done the same.<sup>126</sup>

116. *Continental T.V., Inc. v. GTE Sylvania Inc.*, 694 F.2d 1132, 1138 n.12 (9th Cir. 1982); see *Rickards v. Canine Eye Registration Found., Inc.*, 704 F.2d 1449, 1454 (9th Cir.), *cert. denied*, 104 S. Ct. 488 (1983).

117. See, e.g., *JBL Enters., Inc. v. Jhirmack Enters., Inc.*, 698 F.2d 1011, 1015 (9th Cir.), *cert. denied*, 104 S. Ct. 106 (1983); *Valley Liquors, Inc. v. Renfield Importers, Ltd.*, 678 F.2d 742, 745 (7th Cir. 1982); *Oreck Corp. v. Whirlpool Corp.*, 579 F.2d 126, 131 (2d Cir.), *cert. denied*, 439 U.S. 946 (1978).

118. 461 F. Supp. 1025 (N.D. Tex. 1978).

119. *Id.* at 1027.

120. *Id.* at 1036.

121. *Id.* at 1036 n.4.

122. First, the court observed, "[s]ome decisions have cited *Donovan* but have equally relied upon immunity of instrumentalities of state governments or other immunities." *Id.* at 1037. Second, the court stated, the earlier cases represented an effort to deal with the occasional factual circumstance that ownership of land may,

because of its unique location or other property attributes, give to the landowner a specie of natural monopoly. It supports the idea that a contract that merely transfers exclusivity inherent in the ownership of real property is per se legal.

*Id.* As to the first of the district court's rationales, although some cases do discuss the state action exemption, see cases cited *infra* note 126, many others, including the Supreme Court decisions themselves, do not. As to the court's second rationale, we are in partial agreement but do not believe that there is anything in the reasoning or the facts of the early cases that renders them as limited as the *Woolen* court suggests.

123. 461 F. Supp. at 1040.

124. *Id.* at 1037. One "untoward distinction" identified in *Woolen* was that employed by the Eighth Circuit in *TV Signal Co. v. AT & T*, 462 F.2d 1256 (8th Cir. 1972), which distinguished between cases in which the plaintiff was a competitor of the putative supplier and those in which the plaintiff was a competitor of the exclusive franchisee. See *id.* at 1260. The *Woolen* court stated that "[t]he reality of the found difference is unclear." 461 F. Supp. at 1037. See *infra* note 186 and accompanying text. Another line of cases that *Woolen* may have intended to identify as being inconsistent with the exclusive distributorship precedent involved shopping center restrictive covenants. See 461 F. Supp. at 1037. See *infra* notes 205-08 and accompanying text.

125. 461 F. Supp. at 1040.

126. See, e.g., *MLC, Inc. v. North Am. Philips Corp.*, 1983 Trade Cas. (CCH) ¶ 65,351, at 70,098-99 (S.D.N.Y. May 3, 1983) (denying in part the defendant's motion for summary judgment); *Charley's Taxi Radio Dispatch Corp. v. SIDA of Hawaii, Inc.*, 562

IV. EXCLUSIVE DISTRIBUTION AND *SYLVANIA*

Not since *Bausch & Lomb*,<sup>127</sup> which in effect reaffirmed *Pullman, Ad-dyston*, and *Donovan*,<sup>128</sup> has the Supreme Court ruled on exclusive distribution arrangements. One might therefore argue that under the antitrust laws the legality of exclusive franchising remains intact. On the other hand, one can sympathize with the position of several commentators that *Sylvania* should govern judicial scrutiny of exclusive distribution.<sup>129</sup> As one recent commentator argued: "Exclusive distributorships are simply a particular genre of vertical nonprice restrictions, differing only in superficial respects from the vertical restrictions on customers and territories subjected to per se analysis in *Schwinn*."<sup>130</sup> That argument continues that *Sylvania* contemplated that all nonprice vertical restraints, including exclusive franchising, be examined under the rule of reason for their economic impact.<sup>131</sup>

Given the clarity and soundness of the early Supreme Court decisions, we do not readily concede that *Sylvania* requires exclusive franchising to be tested under the same rule of reason standard applicable to the vertical restraints at issue in that case. One should not lightly subject manufacturers granting exclusive distributorships to expensive and protracted pre-trial discovery or to the trial of a rule of reason case, with its amorphous standard.<sup>132</sup> At the same time, however, we feel obliged to attempt

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F. Supp. 712, 714-15 (D. Hawaii 1983) (denying a motion to dismiss); see also *Konik v. Champlain Valley Physicians Hosp. Medical Center*, 561 F. Supp. 700, 720 (N.D.N.Y. 1983) (denying in part defendant's motion for summary judgment), *aff'd*, 733 F.2d 1007 (2d Cir. 1984), *cert. denied*, 105 S. Ct. 253 (1984); *Cincinnati Riverfront Coliseum, Inc. v. City of Cincinnati*, 556 F. Supp. 664, 667 (S.D. Ohio 1983) (denying summary judgment); *cf. Gold Cross Ambulance & Transfer & Standby Serv., Inc. v. Kansas City*, 705 F.2d 1005, 1017 (8th Cir. 1983) (analysis under the state action immunity rubric), *petition for cert. filed*, 52 U.S.L.W. 3039 (U.S. July 25, 1983) (No. 83-138); *Tom Hudson & Assocs., v. City of Chula Vista*, 746 F.2d 1370, 1374-75 (9th Cir. 1984) (same).

127. *United States v. Bausch & Lomb Optical Co.*, 321 U.S. 707 (1944).

128. See *supra* notes 44-65 and accompanying text.

129. See *Baker, supra* note 8, at 1517; *Elias, supra* note 8, at 439-40.

130. *Baker, supra* note 8, at 1517; *accord Elias, supra* note 8, at 458.

131. *Elias* argues that permissive treatment of exclusive distribution arrangements would be "in irreconcilable conflict" with the Supreme Court's decision in *United States v. Topco Assocs., Inc.*, 405 U.S. 596 (1972), see *Elias, supra* note 8, at 446, and that "[b]y focusing on the relationship between and relative importance of interbrand and intrabrand competition rather than on the form of the arrangement, the Court's rationale [in *Sylvania*] casts doubt on the continued viability of the exclusive franchise precedents," *id.* at 439-40. *Elias* also makes much of the "[c]onspicuous . . . absence" in the Supreme Court's decision in *Sylvania* of reference to the "veritable avalanche" of exclusive dealership precedents "heavily relied upon by the Court of Appeals." *Id.* at 458. See *supra* notes 105, 114 and accompanying text. Although *Elias* is not alone in questioning "the continuing viability of the exclusive dealership cases . . . in the wake of *Topco*," *American Motor Inns, Inc. v. Holiday Inns, Inc.* 521 F.2d 1230, 1244 n.38 (3rd Cir. 1975), we believe the horizontal aspect of *Topco* distinguishes that case from those discussed herein. We discuss in the text how one might reconcile the treatment of exclusive franchising that we urge with *Sylvania*. See *infra* notes 132-41 and accompanying text.

132. See, e.g., *Northern Pac. Ry. Co. v. United States*, 356 U.S. 1, 5 (1958) (observing that a per se rule "avoids the necessity for an incredibly complicated and prolonged eco-



to reconcile what we urge—effectively per se legal treatment of exclusive distribution—and the approach adopted by the Court in *Sylvania*.

The Supreme Court in *Sylvania* employed a “functional economic analysis” and required a showing of “demonstrable economic effect” before holding a nonprice vertical restraint per se unlawful.<sup>133</sup> Applying that requirement to justify a more lenient approach to exclusive distribution presents a problem. A strong argument can be made that the economic analysis set forth in Part II above applies to *all* truly vertical distribution arrangements, including those at issue in *Sylvania*.<sup>134</sup> Accordingly, following the Court’s mandate to use economic analysis causes the very rulings in *Sylvania*, which did not find the vertical restraints involved there to be per se legal, to collapse.

Nor will it suffice to distinguish exclusive franchising by employing the particular species of analysis suggested in *Sylvania*: the inquiry into interbrand and possibly intrabrand competition. The principal difficulty with that analysis is the concept of intrabrand competition. We believe the term is a misnomer. The antitrust laws permit both vertical integration by internal expansion<sup>135</sup> and unilateral refusals to deal.<sup>136</sup> Intrabrand competition turns out to be what exists when a manufacturer decides not to integrate vertically and not to appoint one distributor and unilaterally refuse to deal with all others—in short, when the manufacturer decides to market his goods in one of many possible ways. Intrabrand competition has a precarious, evanescent existence, as “[e]very manufacturer has a natural and complete monopoly of his particular product.”<sup>137</sup> Because it can be extinguished unilaterally, in a real sense intrabrand competition does not exist.<sup>138</sup>

Inquiry into the competitive effects of vertical restraints should focus only on interbrand effects—that is, on competition in the relevant market “as a whole.”<sup>139</sup> When tested under that standard, which is not nec-

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omic investigation into the entire history of the industry involved, as well as related industries”); Posner I, *supra* note 10, at 15 (arguing that the courts are not equipped to apply the Rule of Reason standard); cf. *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 609-10 (1972) (acknowledging the “inability to weigh, in any meaningful sense, destruction of competition in one sector of the economy against promotion of competition in another sector”).

133. 433 U.S. at 59.

134. See Posner I, *supra* note 10, at 18-22; Bork III, *supra* note 25, at 180-82.

135. See *supra* note 48.

136. See *supra* note 12.

137. *Schwing Motor Co. v. Hudson Sales Corp.*, 138 F. Supp. 899, 902 (D. Md.), *aff’d per curiam*, 239 F.2d 176 (4th Cir. 1956), *cert. denied*, 355 U.S. 823 (1957).

138. As one court perceived in examining the grant of an exclusive franchise: “True, there may be some reduction in intrabrand competition, but a manufacturer enjoys a natural monopoly in its own product and no competition in the product line is restrained.” *Woolen v. Surtran Taxicabs, Inc.* 461 F. Supp. 1025, 1038 (N.D. Tex. 1978) (emphasis in original deleted, current emphasis added); see Baker, *supra* note 8, at 1490-93.

139. *Oreck Corp. v. Whirlpool Corp.*, 579 F.2d 126, 133-34 (2d Cir.), *cert. denied*, 439 U.S. 946 (1978); accord, e.g., *Borger v. Yamaha Int’l Corp.*, 625 F.2d 390, 397 (2d Cir.

essarily inconsistent with *Sylvania*,<sup>140</sup> exclusive franchising by itself is harmless. But so are the dealer restraints at issue in *Sylvania*, particularly because no *Sylvania* dealer was prohibited from dealing in the goods of other suppliers.<sup>141</sup>

One might try accepting *Sylvania* on its own terms and attempt to distinguish exclusive franchising from the forms of dealer-based vertical restraints at issue in that case. The endeavor is not terribly fruitful. Perhaps the clearest distinction between exclusive distribution and dealer-based restraints is that the former limits the conduct of only the manufacturer. It is thus not technically a restraint on alienation.<sup>142</sup> Although the idea of restraint on alienation has played a role in antitrust jurisprudence,<sup>143</sup> no cogent explanation has been offered for permitting property law concepts to control the resolution of antitrust disputes.<sup>144</sup>

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1980) (instructing jury that liability could be found "solely on the basis of a purpose to restrict intrabrand competition" constitutes reversible error); *In re Beltone Elecs. Corp.*, 100 F.T.C. 68, 208 (July 6, 1982) ("[I]t is not sufficient for a party challenging a vertical restraint to show only a resultant loss of intrabrand competition. Rather, current judicial precedent indicates that the party must show that the restraint also has a probable adverse effect on interbrand competition."); see *Jefferson Parish Hosp., Dist. No. 2 v. Hyde*, 104 S. Ct. 1551, 1561 (1984); *Indiana Fed'n of Dentists v. FTC*, 1984-2 Trade Cas. (CCH) ¶ 66,299, at 66,926 & n.16 (7th Cir. Oct. 11, 1984); *Cascade Cabinet Co. v. Western Cabinet & Millwork, Inc.*, 1983 Trade Cas. (CCH) ¶ 65,482, at 68,346 (9th Cir. July 5, 1983) (quoting *Gough v. Rossmoor Corp.*, 585 F.2d 381, 389 (9th Cir. 1978), *cert. denied*, 440 U.S. 936 (1979)); *Products Liab. Ins. Agency v. Crum & Forster Ins. Cos.*, 682 F.2d 660, 664 (7th Cir. 1982). But cf. *Graphic Prods. Distribs., Inc. v. Itek Corp.*, 717 F.2d 1560, 1571-72 & nn.18, 20 (11th Cir. 1983) (Reduction in intrabrand competition alone may be sufficient to impose liability.); *Eiberger v. Sony Corp.*, 622 F.2d 1068, 1081 (2d Cir. 1980) (asserting that *Oreck* should be limited to its facts and refusing to find "that anticompetitive impact on intrabrand competition cannot alone" constitute a violation of § 1); *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164, 166 (3d Cir. 1979) (reversing grant of summary judgment).

140. After stating that the Court in *Sylvania* made only a "glancing reference" to "balancing" interbrand and intrabrand effects, Posner states that "[t]he Court did not say that such balancing was the right way to apply the Rule of Reason, but only that it was not impermissibly subjective." Posner I, *supra* note 10, at 18 & n.51. Compare *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 52 n.19 (1977) ("[i]nterbrand competition is . . . the primary concern of antitrust law") with *id.* at 45 (discussing the *Schwinn* Court's determination regarding the "competitive situation in 'the product market as a whole'").

141. As we demonstrate elsewhere, see *supra* note 39, *infra* note 152 and accompanying text, the antitrust laws are adequate to deal directly with interbrand and other horizontal restraints that might accompany exclusive franchising.

142. See *Louis I*, *supra* note 6, at 283; see also *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 46 (1977) ("In both [the *Schwinn* and *Sylvania*] cases the restrictions limited the freedom of the retailer to dispose of the purchased products as he desired.").

143. See *Sylvania*, 433 U.S. at 66-67 (White, J., concurring) (discussing "the notion in many of our cases involving vertical restraints that independent businessmen should have the freedom to dispose of the goods they own as they see fit"); *United States v. Arnold, Schwinn & Co.*, 388 U.S. 365, 377 (1967) ("[R]estraints upon alienation . . . are beyond the power of the manufacturer to impose upon its vendees."); *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373, 404, 407-09 (1911) ("[R]estraint upon alienation is ordinarily invalid.").

144. See *Bork III*, *supra* note 25, at 188-89.

A related argument might claim that because an exclusive distributorship results from the manufacturer's appointment of one distributor and refusal to appoint any others, a manufacturer could effectively create an exclusive distributorship unilaterally and without a formal agreement.<sup>145</sup> In order to bind the dealer in a dealer-restraining arrangement, however, the manufacturer seems to be in greater need of an express agreement. We might try to justify a difference in treatment by distinguishing between those restraints that "had to be" embodied in formal contracts and those that did not.<sup>146</sup> That argument too is not persuasive. It is quite true that section 1 requires concert of action, and we do not subscribe to the view that a series of unilateral acts is sufficient to satisfy the statute.<sup>147</sup> Yet once an agreement exists, there does not appear to be any reason in policy or warrant under statute for inquiring into whether the agreement was somehow not necessary. Furthermore, it is not satisfying to ground distinctions among types of vertical restraints on the concert of action requirement, which is only tangentially related to the pertinent question: What is the actual competitive impact of those arrangements?

A final variation of this argument is that because the exclusive franchise "restrains" only the manufacturer,<sup>148</sup> the benefit of such a franchise to an individual dealer does not depend on whether other dealers have similar agreements. Customer and territorial restraints on dealers, on the other hand, "become benefits only when other dealers are similarly bound."<sup>149</sup> The interdependent conduct of dealers in the dealer restraint situation more closely resembles group action by competitors than does exclusive franchising.<sup>150</sup> Hence, this argument concludes, wholly vertical exclusive franchising can legitimately be accorded more lenient treatment than the more "horizontal looking" dealer restraints such as those at issue in *Sylvania*.

With its emphasis on the difference between vertical and horizontal restraints, that argument might be slightly more appealing in the current judicial climate.<sup>151</sup> It does, however, seem contrived to distinguish

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145. See *supra* note 12.

146. Cf. Vertical Guidelines, *supra* note 10, at 7 (attempting to differentiate intrabrand restraints from horizontal, interbrand restraints by noting that interbrand "restraints can have no effect that could not also be obtained through the unilateral action of the manufacturer of the particular brands in question").

147. See Baker, *supra* note 8, at 1474 ("It does not strain common usage to find concerted action where systematic refusals to deal are used successfully as bludgeons to compel compliance with announced policy."). For general discussions of the concerted action requirement, see Bauer, *Per Se Illegality of Concerted Refusals to Deal: A Rule Ripe for Reexamination*, 79 Colum. L. Rev. 685, 691 (1979); Comment, *Vertical Agreement as Horizontal Restraint: Cernuto, Inc. v. United Cabinet Corp.*, 128 U. Pa. L. Rev. 622, 628 (1980).

148. Cf. L. Sullivan, *supra* note 1, at 426 ("The distinction between a seller's promise and a buyer's is perhaps a practical, if clumsy, place to draw the line."). See *supra* note 13.

149. Louis I, *supra* note 6, at 286.

150. *Id.*

151. The courts routinely describe distributional restraints as emanating from either

among vertical restraints on the basis of how closely they resemble horizontal group activity. Horizontal group activity of the kind discussed here is per se unlawful.<sup>152</sup> Purely vertical activity, even if it somehow resembles horizontal activity, is not.<sup>153</sup>

A more persuasive ground for distinguishing exclusive franchising from the dealer-based restraints at issue in *Sylvania* might lie in the analogy to vertical integration by internal expansion. As we saw, the Supreme Court decisions upholding exclusive distribution rely on that analogy.<sup>154</sup> It might be argued that the appointment of an exclusive distributor more closely resembles vertical integration by internal expansion, which is permissible under the antitrust laws,<sup>155</sup> than any other vertical restraint. The argument might continue that it is with the appointment of an exclusive distributor that a court can most clearly presume a consonance of interests between manufacturer and consumer. The fact that a company grants an exclusive distributorship rather than expands internally demonstrates the manufacturer's belief that the arrangement enhances efficiency. Such a decision merits judicial deference, particularly because no sound basis exists for giving an artificial incentive to internal expansion.<sup>156</sup> It is true, of course, that other vertical arrangements can also fairly be likened to vertical integration by internal expansion, and the efficiency explanation discussed above applies to them as well. In the final analysis, we are dealing only with differences in degree.

None of the distinctions suggested above is compelling. Taken together, however, they should be enough to convince even the relatively cautious that dismissal at the pleading stage of challenges to exclusive franchise agreements—dismissal without a full-blown investigation

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"horizontal" or "vertical" agreements and permit significant differences in antitrust enforcement to turn on the different nomenclature used. See *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 57 & n.27 (1977); see also *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 608 (1972) ("We think that it is clear that the restraint in this case is a horizontal one, and, therefore, a *per se* violation of § 1."); *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164, 168 (3d Cir. 1979) (horizontal nature of distributional restraint would merit per se treatment). On the overuse of the horizontal/vertical distinction, see Posner I, *supra* note 10, at 22-26; Bork III, *supra* note 25, at 189-91. See *supra* note 131.

152. *United States v. Topco Assocs., Inc.*, 405 U.S. 596, 608 (1972); cf. *Cernuto, Inc. v. United Cabinet Corp.*, 595 F.2d 164, 166 (3d Cir. 1979) (describing behavior subject to per se illegality). See *supra* note 39.

153. See *supra* notes 107-15, 151-52 and accompanying text.

154. See *supra* notes 49, 57-58 and accompanying text.

155. See cases cited *supra* note 48.

156. See *supra* note 49. See, e.g., *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 57 n.26 (1977) (rejecting application of per se rule to the vertical restraints before the Court because applying that standard would "creat[e] an incentive for vertical integration into the distribution system, thereby eliminating to that extent the role of independent businessmen"); *Red Diamond Supply, Inc. v. Liquid Carbonic Corp.*, 637 F.2d 1001, 1007 (5th Cir.) ("[S]ince [the defendant] could have accomplished these ends by either internal expansion or merger, either of which would have had an even greater impact on intrabrand competition, we fail to see why it would have been unreasonable for [the defendant] to accomplish the same ends by contract."), *cert. denied*, 454 U.S. 827 (1981).

under the rule of reason—is not inconsistent with the letter or spirit of even a broad reading of *Sylvania*. Such dismissal is fully supported by economic analysis and by the line of Supreme Court authority upholding exclusive franchising. Ultimately, though, *Sylvania* should be modified. Elevating interbrand competition from the primary to the sole concern of the antitrust laws, which a number of courts have in effect already done,<sup>157</sup> is all that is required to place exclusive franchising beyond challenge. Consistency with the full implications of the analysis set out in Parts II and III above may well require more.<sup>158</sup>

## V. APPLICATION OF EXCLUSIVE DISTRIBUTION THEORY

The economic and legal principles discussed above may be helpful in analyzing the antitrust implications of a number of business arrangements that are the subject of much litigation today.

### A. *Transportation Services*

The owner or operator of a transportation facility such as a railway station or an airport may find it beneficial to grant to a single firm the right to service the facility. The scenario is familiar; it is the factual setting that gave rise to the Supreme Court holdings on exclusive distribution.<sup>159</sup>

If the firm controlling the facility is a profit maximizer, it acts on the basis of self-interest; if it is a municipal or other public authority, it acts pursuant to its mandate to further the public interest.<sup>160</sup> In either case the decisionmaker and the consumers have a commonality of interests in maximizing the efficient distribution of the product or service in question. Courts analyzing such exclusive franchises should therefore find them lawful.<sup>161</sup> As the Supreme Court ruled in *Donovan*, the antitrust laws do not require a railroad company to appoint multiple franchisees simply because it appointed one.<sup>162</sup> Who provides the service is “a matter of indifference to the public.”<sup>163</sup>

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157. See *supra* note 139 and accompanying text.

158. See, e.g., R. Bork, *supra* note 7, at 288-91; Bork III, *supra* note 25, at 190-92; Posner I, *supra* note 10, at 22-26.

159. See *Donovan v. Pennsylvania Co.*, 199 U.S. 279 (1905). See *supra* notes 44-68 and accompanying text.

160. See *supra* notes 38-39, 54 and accompanying text.

161. But cf. cases cited in note 126 *supra*.

162. See *Donovan v. Pennsylvania Co.*, 199 U.S. 279, 296 (1905) (“The railroad company was not bound to accord this particular privilege [of being a franchisee] to the defendants simply because it had accorded a like privilege to the Parmelee Transfer Company”). See *supra* notes 59-65 and accompanying text.

163. *Chicago, St. L. & N.O. R.R. v. Pullman S. Car Co.*, 139 U.S. 79, 89 (1891). See *supra* notes 44-54 and accompanying text.

### B. Sports Stadiums and Other "Essential Facilities"

In *Twin City Sportservice, Inc. v. Charles O. Finley & Co.*,<sup>164</sup> Sportservice alleged that Finley had breached a concession agreement. Finley counterclaimed, alleging that the contract violated sections 1 and 2 of the Sherman Act. By the terms of the agreement, Penn, a predecessor in interest of Sportservice, obtained from the owner of Shibe Park and the Philadelphia Athletics baseball team a fifteen-year exclusive concession franchise for all events at the park, including home games played by the Athletics.<sup>165</sup> The contract provided that the concession was to be "unaffected by change of ownership" of the park,<sup>166</sup> and a subsequent modification provided that Sportservice's franchise would continue both at Shibe Park and at any new location to which the Athletics might move.<sup>167</sup> After a number of other modifications, the franchise term was extended to thirty-three years.<sup>168</sup>

Although the agreement bound the park owner not to deal with any concessionaire other than Sportservice's predecessor, Sportservice remained free to attempt to gain the concession at other sports or recreational facilities. Sportservice succeeded in acquiring exclusive franchises at a number of other facilities. In part because of that "pattern of contractual relations"<sup>169</sup> and in part because of the duration of the franchise agreements<sup>170</sup> the Ninth Circuit affirmed the district court's conclusion that the contract with Finley unreasonably restrained trade.<sup>171</sup> The court of appeals also affirmed the finding that "both franchisors and concessionaires have been foreclosed from competition in the relevant market."<sup>172</sup>

Although it is clear from the opinions that discrete competitors were outcompeted by Sportservice, it is difficult to understand how competition in any relevant market was diminished or how consumers were ill-served. The Ninth Circuit noted with disapproval that "in many instances the long-term contracts were procured by Sportservice's cash

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164. 365 F. Supp. 235 (N.D. Cal. 1972), *rev'd and remanded*, 512 F.2d 1264 (9th Cir. 1975), *on appeal after remand*, 676 F.2d 1291 (9th Cir.), *cert. denied*, 459 U.S. 1009 (1982).

165. 512 F.2d at 1268.

166. *Id.* (quotation marks in original).

167. *Id.* at 1269.

168. *Id.*

169. 676 F.2d at 1303; *see id.* at 1303-05, 1308.

170. *Id.* at 1305-06.

171. *Id.* at 1305.

172. *Id.* at 1304. The court of appeals analyzed the contract at issue under the "exclusive dealing" line of cases, the structural format of which is more stringent than even the rule of reason standard adumbrated in *Sylvania*. *See supra* notes 15, 17. There is an essential symmetry between exclusive dealing and exclusive distribution. *See Vertical Guidelines, supra* note 10, at 19-20. *See supra* note 17 and accompanying text. Although the distinctions proffered above, *see supra* notes 17, 142-56 and accompanying text, may adequately distinguish exclusive distribution from exclusive dealing, we believe that there exists a fundamental conflict between what we maintain is the proper standard by which to judge exclusive distribution and the exclusive dealing lines of cases.

payment loans or other financial inducements."<sup>173</sup> But the antitrust laws should not discourage such conduct. The only difference between the facts in *Twin City* and a classic exclusive distribution arrangement is that Sportservice was able to procure a number of exclusive franchises. That conduct, however, does not harm competition.<sup>174</sup> It results *from* competition and is beneficial to consumers.<sup>175</sup> Regardless of the duration of the franchise,<sup>176</sup> each transaction between franchisee and individual stadium owner will endeavor to minimize the costs of distribution and will result in the most efficient allocation of resources under the circumstances.<sup>177</sup> It is difficult to understand how the cumulation of socially optimal arrangements could result in a net or long-term diminution in consumer welfare. One might claim that if the exclusive franchisee acquires many long-term franchises other potential franchisees would leave the business, and when the franchises come up for renewal there would be a dearth of potential franchisees with whom the stadium owners could negotiate. Even in such a situation, however, the stadium owners would be able to control the competitive activity of the franchisee.<sup>178</sup> As we noted above,<sup>179</sup> the owners might miscalculate and fail to preclude or stop pricing abuses by the franchisee. But in such a case the owners, like the public, would be worse off, and they would correct their error. Such mistakes should not form the basis of antitrust complaints.<sup>180</sup>

The stadium concession in *Twin City* has characteristics similar to other businesses that operate "scarce facilities,"<sup>181</sup> which an increasing number of courts mistakenly denominate "essential facilities" or "essen-

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173. *Twin City*, 676 F.2d at 1308.

174. As the Supreme Court stated in *Pullman*:

We cannot perceive that such a contract is at all in restraint of trade. The plaintiff [franchisee] was at liberty, so far as that contract was concerned, to make similar arrangements for the accommodation of passengers on all other railroads in the country, even those that are rivals or competitors in business with the defendant [railroad].

*Chicago, St. L. & N.O. R.R. v. Pullman S. Car Co.*, 139 U.S. 79, 89 (1891).

175. The parties in *Twin City* had stipulated that the exclusive arrangement was "the only practical way to conduct the business of concession sales at the events and facilities involved." 676 F.2d at 1306 n.12. The Ninth Circuit, however, refused to render a "judgment as to the propriety of the exclusive nature of the franchise agreements." *Id.* Reflecting upon what it was doing, the court of appeals noted a "certain irony" about its holding:

While our decision here may promote competition in the concession franchise market, the unchallenged pragmatic monopolies created by these exclusive agreements will probably prevent this decision from having much effect upon the price of the spectator's next hot dog.

*Id.*

176. See *supra* note 42 and accompanying text.

177. See *supra* notes 36-38 and accompanying text.

178. See *supra* notes 31-36 and accompanying text.

179. See *supra* notes 29-30, 39, 42 and accompanying text.

180. See *supra* notes 37-38, 42 and accompanying text.

181. *Aspen Highlands Skiing Corp. v. Aspen Skiing Co.*, 738 F.2d 1509, 1519 (10th Cir.) (quoting *Byars v. Bluff City News Co.*, 609 F.2d 843, 856 (6th Cir. 1980)), *cert. granted*, 53 U.S.L.W. 3413 (U.S. Dec. 3, 1984).

tial services.”<sup>182</sup> Related to the “bottleneck principle” as applied to a monopolist’s or dominant firm’s refusal to deal,<sup>183</sup> the essential facility doctrine is the newest guise in which competitors seeking to protect themselves from the rigors of competition have sought to cloak themselves.

The elements necessary to establish liability under the essential facility doctrine are generally stated to be: “(1) control of the essential facility by a monopolist; (2) a competitor’s inability practically or reasonably to duplicate the essential facility; (3) the denial of the use of the facility to a competitor; and (4) the feasibility of providing the facility.”<sup>184</sup> We limit the present discussion to cases in which the refusal to deal is the consequence of the grant of an exclusive franchise by the owner of the essential facility to a competitor of the plaintiff.<sup>185</sup> We thereby exclude cases involving challenges by a competitor of the owner of the essential facility<sup>186</sup>

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182. See, e.g., *id.*; MCI Communications Corp. v. AT & T, 708 F.2d 1081, 1148 (7th Cir.), *cert. denied*, 104 S. Ct. 234 (1983).

183. See, e.g., Byars v. Bluff City News Co., 609 F.2d 843, 856-58 (6th Cir. 1980); Poster Exch., Inc. v. National Screen Serv. Corp., 431 F.2d 334, 338-39 (5th Cir. 1970), *cert. denied*, 401 U.S. 912 (1971); Becker v. Egypt News Co., 548 F. Supp. 1091, 1097 (E.D. Mo. 1982), *aff’d*, 713 F.2d 363 (8th Cir. 1983); Note, *Refusals to Deal by Vertically Integrated Monopolists*, 87 Harv. L. Rev. 1720, 1740-52 (1974). For Supreme Court consideration of this issue, see Otter Tail Power Co. v. United States, 410 U.S. 366, 377-79 (1973).

184. MCI Communications Corp. v. AT & T, 708 F.2d 1081, 1132-33 (7th Cir.), *cert. denied*, 104 S. Ct. 234 (1983), *cited in* Aspen Highlands Skiing Corp. v. Aspen Skiing Co., 738 F.2d 1509, 1520 (10th Cir.), *cert. granted*, 53 U.S.L.W. 3413 (U.S. Dec. 3, 1984); *accord*, e.g., Hecht v. Pro-Football, Inc., 570 F.2d 982, 992-93 (D.C. Cir. 1977) (analysis under §§ 1, 2 & 3), *cert. denied*, 436 U.S. 956 (1978); City of Chanute v. Kansas Gas & Elec. Co., 564 F. Supp. 1416, 1421-22 (D. Kan. 1983) (analysis under § 2); Southern Pac. Communications Co. v. AT & T, 556 F. Supp. 825, 974-75 & n.181 (D.D.C. 1983) (same), *aff’d*, 740 F.2d 980 (D.C. Cir. 1984); Mid-South Grizzlies v. NFL, 550 F. Supp. 558, 569-70 & n.28 (E.D. Pa. 1982) (analysis under § 1), *aff’d*, 720 F.2d 772, 787 (3d Cir. 1983), *cert. denied*, 104 S. Ct. 2657 (1984); United States v. AT & T, 524 F. Supp. 1336, 1352-53 (D.D.C. 1981) (analysis under § 2), *aff’d per curiam*, 714 F.2d 178 (D.C. Cir. 1983); see Smith v. Northern Mich. Hosps., Inc., 703 F.2d 942, 953 (6th Cir. 1983); Interface Group, Inc. v. Gordon Publications, Inc., 562 F. Supp. 1235, 1242-43 (D. Mass. 1983).

185. See, e.g., Byars v. Bluff City News Co., 609 F.2d 843, 856-59 (6th Cir. 1980); Hecht v. Pro-Football, Inc., 570 F.2d 982, 985-86 (D.C. Cir. 1977), *cert. denied*, 436 U.S. 956 (1978).

186. See, e.g., Otter Tail Power Co. v. United States, 410 U.S. 366, 377-79 (1973); Lorain Journal Co. v. United States, 342 U.S. 143, 152-55 (1951); R. Bork, *supra* note 7, at 344-46. We do not believe that a radically different analysis should be applied in the case of a refusal to deal with a competitor of the owner. Cf. *supra* note 124. Recall that *Addyston* reasoned to the conclusion that the railroad could protect from competition the franchisee sleeping-car company from the proposition that in discharging its duty the railroad could have protected *itself* from such competition. See *supra* notes 55-58, 64-65 and accompanying text. See NFL v. North Am. Soccer League, 459 U.S. 1074, 1079 (1982) (Rehnquist, J., dissenting from denial of certiorari) (“The Court of Appeals seems to me to have implicitly adopted the view that businesses must arrange their affairs so as to make it possible for would-be competitors to compete successfully. This Court has explicitly stated the contrary: The inquiry under the Rule of Reason is concerned only with ‘impact on competitive conditions.’” (quoting National Soc’y of Professional Eng’rs



and cases involving essential facilities operated by a group of competitors who exclude the plaintiff from effective competition with the group.<sup>187</sup> Assuming the owner or operator of the essential facility is a profit maximizer, it is goaded by incentives that guarantee maximization of consumer welfare. The grant by such an owner of an exclusive franchise to the plaintiff's competitor should be examined under the exclusive distribution analysis discussed herein<sup>188</sup> and should be found lawful.<sup>189</sup>

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v. United States, 435 U.S. 679, 688, 690 (1978)); *Northeastern Tel. Co. v. AT & T*, 651 F.2d 76, 93 (2d Cir. 1981) ("[A] monopolist's right to compete is not limited to actions undertaken with an altruistic purpose. Even monopolists must be allowed to do as well as they can with their business."), *cert. denied*, 455 U.S. 943 (1982); *Official Airline Guides, Inc. v. FTC*, 630 F.2d 920, 925 (2d Cir. 1980) ("[S]ection 2 of the Sherman Act does not forbid a monopolist from ever acting in its own self-interest.") (emphasis added), *cert. denied*, 450 U.S. 917 (1981); *Southern Pac. Communications Co. v. AT & T*, 556 F. Supp. 825, 974-75 & n.181 (D.D.C. 1982) (applying exclusive distribution analysis to a refusal to deal with a potential competitor), *aff'd*, 740 F.2d 980 (D.C. Cir. 1984). *But cf. Unclogging the Bottleneck*, *supra* note 53, at 441-42 (proposing a unified standard—which we maintain is inconsistent with the fundamental principles of antitrust law discussed herein, see *supra* notes 51-54, 58 and accompanying text—for competitors as well as for customers and suppliers of the essential facility).

187. See, e.g., *Associated Press v. United States*, 326 U.S. 1, 17-18 (1945); *United States v. Terminal R.R. Ass'n*, 224 U.S. 383, 405, 409 (1912); *Gamco, Inc. v. Providence Fruit & Produce Bldg., Inc.*, 194 F.2d 484, 487 (1st Cir.), *cert. denied*, 344 U.S. 817 (1952); 3 P. Areeda & D. Turner, *supra* note 20, ¶ 729g; R. Posner, *supra* note 34, at 211; L. Sullivan, *supra* note 1, at 130-31; see also *Unclogging the Bottleneck*, *supra* note 53, at 470-71 (urging that the same standard be applied to unilateral and joint refusals to deal). The court in *Byars v. Bluff City News Co.*, 609 F.2d 843 (6th Cir. 1980), euphemistically noted the "tension" between these cases and exclusive distributorship theory. *Id.* at 858 n.39.

188. See *supra* Parts II and III.

189. See *Continental Cablevision v. American Elec. Power Co.*, 715 F.2d 1115, 1120-21 (6th Cir. 1983) (analysis under § 2); *Smith v. Northern Mich. Hosps., Inc.*, 703 F.2d 942, 954-55 (6th Cir. 1983) (same). See also *Official Airline Guide, Inc. v. FTC*, 630 F.2d 920, 925-28 (2d Cir. 1980), *cert. denied*, 450 U.S. 917 (1981), which reasons to the same conclusion by means of a different analysis. One might attempt to distinguish between the essential facility doctrine and exclusive distribution theory by asserting that the former requires an under-utilization of capacity before the owner of the essential facility would be forced to deal. See *supra* note 184 and accompanying text. (Note that the Supreme Court in *Pullman*, in upholding the exclusivity arrangement before it, spoke of the "requisite number" of facilities being available by virtue of the service rendered by the exclusive franchise. See *Chicago St. L. & N.O. R.R. v. Pullman S. Car Co.*, 139 U.S. 79, 89 (1891). See *supra* note 47 and accompanying text.) One seeking to justify the current state of the law regarding essential facilities might therefore maintain that the forced dealing contemplated by the essential facility doctrine does only good, because the increased use of the facility will increase output and result in a net benefit to consumers. See *supra* notes 24, 29-36 and accompanying text.

Even assuming that the courts applied a consistent meaning of "under-utilization of capacity" before calling into play the essential facility doctrine, we do not believe that difference justifies forced dealing in the essential facility cases. Forced dealing in the circumstances posited would create inefficiencies and disadvantage consumers. See *supra* notes 37-39 and accompanying text. Any firm with market power underutilizes its capacity by restricting its output, yet the courts have not declared forced dealing to be the appropriate response in the nonessential facility context. See cases cited *supra* note 187. Like any other profit maximizer, the owner of the essential facility will have miscalculated if he permits the franchised user to restrict use of the facility without achieving any

### C. Hospital Exclusive Service Agreements

Hospitals commonly engage a single firm or practitioner to provide in-hospital anesthesiology, radiology, or pathology services.<sup>190</sup> Excluded physicians frequently challenge the exclusivity of those arrangements as violative of sections 1 or 2 of the Sherman Act.

The facts of *Jefferson Parish Hospital District No. 2 v. Hyde*<sup>191</sup> are typical. Plaintiff Hyde was a board-certified anesthesiologist who sought admission to practice in East Jefferson General Hospital.<sup>192</sup> The credentials committee of the hospital favorably recommended Hyde, and the hospital's executive committee recommended to the hospital board that Hyde's application be approved.<sup>193</sup> The board, which had authority to make "the ultimate determination with regard to the appointments of physicians to the medical staff,"<sup>194</sup> denied Hyde's application; the hospital had an arrangement with Roux and Associates whereby Roux provided all anesthesia services at East Jefferson.<sup>195</sup> Hyde claimed that the hospital's agreement with Roux violated section 1.

The district court entered judgment for the hospital, but the Fifth Circuit reversed, ruling that the arrangement constituted unlawful tying.<sup>196</sup> Although the Supreme Court reversed that holding, it is instructive for present purposes to consider the position that the Department of Justice and the Federal Trade Commission (FTC) took in urging reversal. The Department and the FTC argued that the structural and relatively strict exclusive dealing precedents were the most appropriate in analyzing the competitive impact of the hospital's exclusive arrangement with Roux.<sup>197</sup>

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compensating efficiencies that benefit the owner and consumers. Forced dealing should not be the response in that situation any more than in any other.

190. E.g., P. Feldstein & C. Roehrig, *An Analysis of Exclusive Contracts and Closed Staffing in Hospitals: The Effect of Competition 3-4* (Report to the Federal Trade Commission May 1982); Rich, *Medical Staff Privileges and the Antitrust Laws*, 2 Whittier L. Rev. 667, 670 (1980); see Kissam, Webber, Bigus, & Holzgraefe, *Antitrust and Hospital Privileges: Testing the Conventional Wisdom*, 70 Calif. L. Rev. 595, 598-99, 652, 663 (1982) [hereinafter cited as *Hospital Privileges*]. For general discussions of hospital practices and the antitrust laws, see Dolan & Ralston, *Hospital Admitting Privileges and the Sherman Act*, 18 Hous. L. Rev. 707 (1981); Drexel, *The Antitrust Implications of the Denial of Hospital Staff Privileges*, 36 U. Miami L. Rev. 207 (1982); Horan & Nord, *Application of Antitrust Law to the Health Care Delivery System*, 9 Cum. L. Rev. 685 (1979).

191. 104 S. Ct. 1551 (1984).

192. *Hyde v. Jefferson Parish Hosp. Dist. No. 2*, 513 F. Supp. 532, 535-37 (E.D. La. 1981), *rev'd*, 686 F.2d 286 (5th Cir. 1982), *rev'd*, 104 S. Ct. 1551 (1984).

193. *Id.* at 537.

194. *Id.* at 535.

195. *Id.* at 536.

196. 686 F.2d at 294-95.

197. See Brief for the United States as Amicus Curiae of Petition for a Writ of Certiorari at 5, *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 104 S. Ct. 1551 (1984) [hereinafter cited as *Brief on Petition for Certiorari*]; Brief for the United States as Amicus Curiae in Support of Reversal at 7-11, *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 104 S. Ct. 1551 (1984).

We note that the case in the district court did concern an exclusive services contract

Dictum appearing near the end of the Supreme Court's opinion can be read as adopting the government's approach.<sup>198</sup>

Is there any reason not to analyze *Hyde* as a case in which the hospital granted Roux an exclusive franchise? We do not believe so. Perhaps more clearly than in other staff privilege cases,<sup>199</sup> the board's refusal to grant Hyde privileges did not result from any combination or conspiracy among hospital staff physicians. Not only did the credentials and executive committees recommend Hyde's admission, but Roux, the exclusive franchisee, testified that anesthesia practice at the hospital should be open to all.<sup>200</sup> In determining how best to staff its anesthesia department, the hospital could have appointed a number of anesthesiologists or could have hired its own. Assuming the hospital were a profit maximizer,<sup>201</sup> its decision to appoint an exclusive agent to carry out the anesthesia services at the hospital would not harm competition. It might "foreclose" a competitor, but concern for such foreclosure is contrary to the fundamental purposes of antitrust.<sup>202</sup> The FTC has stated that "exclusive contracts may affect both competition among physicians and hospitals for patients and competition among physicians to market their services to hospitals."<sup>203</sup> In the latter sense, of course, there was competition among

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between Roux and the hospital. See 513 F. Supp. at 536-38. The point was not addressed by the district court and apparently was not raised on appeal. Query whether plaintiff Hyde would have had standing to complain about an exclusive dealing contract. See *Bowen v. New York News, Inc.*, 522 F.2d 1242, 1255-56 (2d Cir. 1975), *cert. denied*, 425 U.S. 936 (1976).

198. See *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 104 S. Ct. 1551, 1567-68 & nn.47-48, 51-52 (1984).

199. See, e.g., *Robinson v. Magovern*, 521 F. Supp. 842, 904-08 (W.D. Pa. 1981) (rejecting group boycott analysis), *aff'd mem.*, 688 F.2d 824 (3d Cir.), *cert. denied*, 459 U.S. 971 (1982); *McMorris v. Williamsport Hosp.*, 1984-2 Trade Cas. (CCH) ¶ 66,252, at 66,092-94 (M.D. Pa. Sept. 25, 1984) (same); Fed. Trade Comm'n, Enforcement Policy with Respect to Physician Agreements to Control Medical Prepayment Plans 6-10 (1981) (treating differently unilateral hospital staffing decisions and decisions inspired and coerced by physicians acting collusively); *Antitrust and Alternative Health Care Systems*, Address by Walter T. Winslow, Deputy Director, FTC Bureau of Competition, before the Antitrust and Health Care Sections of the Minnesota State Bar Ass'n 10-17 (May 25, 1983) (discussing privilege decisions controlled by a medical staff); *Hospital Privileges*, *supra* note 190, at 603, 651-55 (vulnerability of physician cartels to antitrust challenge).

200. See *Hyde v. Jefferson Parish Hosp. Dist. No. 2*, 686 F.2d 286, 288 n.2 (5th Cir. 1982), *rev'd*, 104 S. Ct. 1551 (1984); see also *McMorris v. Williamsport Hosp.*, 1984-2 Trade Cas. (CCH) ¶ 66,252, at 67,093 n.13 (M.D. Pa. Sept. 25, 1984) (rejecting claim of conspiracy in part because "final authority on the subject of exclusivity rested with the board of managers and not the medical staff").

201. Although "[t]here are a number of different theories of the determinants of hospital behavior . . . [o]ne such theory is that hospitals are profit maximizers." P. Feldstein & C. Roehrig, *supra* note 190, at 6. Even were hospitals "quantity (sales) maximizers and/or quality maximizers where quality is defined as both more inputs for given services as well as additional services," *id.*, they have characteristics of profit-making enterprises, and the analysis in the text would hold true. See *id.* at 10-11, 16-18.

202. See *supra* notes 50-54 and accompanying text.

203. *In re Burnham Hosp.*, [1979-1983 Transfer Binder] Trade Reg. Rep. (CCH) ¶ 22,005, at 22,580 (Feb. 24, 1983) (FTC advisory opinion); *accord*, *Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 104 S. Ct. 1551, 1567-68 & n.51 (1984).

hackmen to transport passengers from Union Station, but the Supreme Court in *Donovan* dismissed such "competition" as irrelevant to the anti-trust inquiry.<sup>204</sup>

#### D. *Exclusivity Clauses in Shopping Center Leases*

In order to compete more effectively, real estate developers may find it profitable to grant a major or flagship tenant the exclusive right to retail certain goods in a particular shopping center. Legal commentators have urged that such exclusive lease provisions should be declared illegal per se.<sup>205</sup> We disagree.

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204. See *Donovan v. Pennsylvania Co.*, 199 U.S. 279, 294-97 (1905) (The railroad was "under no obligation to refrain from using its property to the best advantage of the public and of itself. It [was] not bound to so use its property that others, having no business with it, may make [a] profit to themselves."). See *supra* text accompanying notes 51-54, 59-65. See also *Car Carriers, Inc. v. Ford Motor Co.*, 1984 Trade Cas. (CCH) ¶ 66,220, at 66,910 (7th Cir. Oct. 2, 1984) ("Losing business to a competitor is an inevitable consequence of the economic system that the Sherman Act was designed to protect; some enterprises will prevail and others will not, but it is the function of § 1 to compensate the unfortunate only when their demise is accompanied by a generalized injury to the market."); *Roland Mach. Co. v. Dresser Indus., Inc.*, 1985-1 Trade Cas. (CCH) ¶ 66,329, at 64,544 (7th Cir. Dec. 21, 1984) ("The exclusion of one or even several competitors, for a short time or even a long time, is not *ipso facto* unreasonable. The welfare of a particular competitor who may be hurt as the result of some trade practice is the concern not of the federal antitrust laws . . . but of state unfair competition law") (citations omitted); *Konik v. Champlain Valley Physicians Hosp.*, 733 F.2d 1007, 1015 (2d Cir. 1984) ("it is the nature of competition that at some point there are winners and losers, and the losers are excluded"); *Marrrese v. American Academy of Orthopaedic Surgeons*, 706 F.2d 1488, 1497 (7th Cir. 1983) (on rehearing) ("[T]hough there is a sense in which the exclusion of any competitor reduces competition, it is not the sense of competition that is relevant to antitrust law."), *rev'd on other grounds*, 736 F.2d 1150 (7th Cir.) (en banc), *rev'd on other grounds*, 53 U.S.L.W. 4265 (U.S. Mar. 4, 1985) (No. 83-1452); *Cascade Cabinet Co. v. Western Cabinet & Millwork Inc.*, 710 F.2d 1366, 1373 (9th Cir. 1983) ("Although Cascade [the plaintiff] complains of its business losses, economic injury to a competitor does not equal injury to competition."); *Berkey Photo, Inc. v. Eastman Kodak Co.*, 603 F.2d 263, 273 (2d Cir.) ("We must always be mindful lest the Sherman Act be invoked perversely in favor of those who seek protection against the rigors of competition."), *cert. denied*, 444 U.S. 1093 (1980).

One might argue that the proper way to view the hospital/physician relationship is to consider the hospital the distributor of services and the physician the supplier. On that assumption, an exclusive arrangement between the hospital and a group of physicians could be said to resemble an exclusive dealing contract. The argument highlights the tension between exclusive dealing and exclusive franchising. See *supra* notes 17, 172. For present purposes, however, we note that in *Hyde* the hospital bore the responsibility of providing anesthesiology services to patients and owned and controlled the facilities at which Hyde wished to work. It is in that regard like the railway station in *Donovan* and the railroad company in *Pullman*. Moreover, the premise of the argument is inconsistent with the position taken by both the Department and the FTC, which, in arguing against the Fifth Circuit's tying rationale, maintained that the supplier or seller was the hospital, not the physicians. See Brief on Petition for Certiorari, *supra* note 197, at 6.

205. See Note, *The Antitrust Implications of Restrictive Covenants in Shopping Center Leases*, 86 Harv. L. Rev. 1201, 1238 (1973) [hereinafter cited as *Antitrust Implications*]; cf. Steuer, *supra* note 9, at 12 ("Exclusives which do not involve distributors, such as shopping center exclusives, do not involve the same procompetitive effects and are more vulnerable" to antitrust attack than exclusive distributorships imposed by a manufac-

Shopping center developments are generally privately owned and managed.<sup>206</sup> It is in the developer's profit-maximizing interest to have the shopping center as attractive to consumers as possible. Achieving that goal may in some circumstances call for a number of tenants selling the same brands or products in order to facilitate comparison shopping. In other cases, the developer might find it more profitable to limit his own freedom of choice and grant to a tenant the equivalent of an exclusive franchise. Whether the developer reaps his share of the value of the lease by lump sum payments or by sharing a portion of the tenant's revenues or profits, the developer wishes the tenant to price and sell as efficiently as possible. The developer would not permit the tenant to add monopoly rents on top of what the developer calculates to be the price-output combination that will maximize the developer's profits, for doing so would enrich the tenant at the expense of the developer.<sup>207</sup> Because the developer is influenced by the same factors that promote consumer welfare, exclusive distribution theory should apply. Far from being per se unlawful, the practice of granting exclusive tenancies should be per se lawful.<sup>208</sup>

### CONCLUSION

Exclusive distribution should be per se lawful under the antitrust laws. Derived from economic analysis and a line of Supreme Court authority, the primary reason for upholding exclusive franchising is that that method of distribution cannot harm competition. When the decision to grant an exclusive franchise is made by a firm acting in its own self-interest, consumer welfare is protected to a greater extent than any ad hoc decisionmaking by a court could secure. A subsidiary rationale for sanctioning exclusive franchising is the common sense notion that courts should not provide artificial, nonmarket incentives for internal expansion, an alternative to exclusive distribution that will be inefficiently pursued if appointments of exclusive distributors are met with expensive and

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turer.); *Harold Friedman Inc. v. Thorofare Mkts. Inc.*, 587 F.2d 127, 140-41 (3rd Cir. 1978) (exclusivity clause in shopping center lease subject to rule of reason analysis); *Countrie Butcher Shoppe, Inc. v. Foodarama Supermarkets, Inc.*, 1982-83 Trade Cas. (CCH) ¶ 65,036, at 70,778 (E.D. Pa. 1982) (same); *Pay Less Drug Stores Northwest, Inc. v. City Products Corp.*, 1975-2 Trade Cas. ¶ 60,385, at 66,678 (D. Or. 1975) (same).

206. *Antitrust Implications*, *supra* note 205, at 1240.

207. See *supra* notes 29-30, 37, 42 and accompanying text.

208. To the extent various department stores, or brands sold by them, compete, does the exclusive contract in some sense effect a diminution in interbrand competition? In the example posited, with competition among developers for consumers' patronage, or with even a monopolist, profit-maximizing developer, the department stores take on characteristics of the sleeping-car companies in *Pullman* and *Addyston* and of the hackmen in *Donovan*. As the Note arguing for per se illegal treatment of exclusive tenancies states: "The exclusionary provisions would thus appear to be vertical restraints that are independently obtained as a result of the dynamics of the negotiating process and the relative bargaining powers of the parties." *Antitrust Implications*, *supra* note 205, at 1214 (footnote omitted). That is all a court should need to know before applying exclusive distribution theory and placing such business arrangements beyond antitrust attack.

protracted challenges under the antitrust laws. Further support is found in the view that complaints of "foreclosure" are typically made by those who seek to further the interests of discrete competitors at the expense of competition and consumer welfare.

Rational use of exclusive distribution maximizes competition and consumer welfare, and courts or antitrust enforcement agencies elevating the short-term pecuniary interests of discrete competitors do so in disregard of the fundamental goals of antitrust. Such social administration is costly in many ways. It does not simply benefit a litigant without affecting competition; it infuses inefficiency into the competitive process and diminishes the very public welfare that courts and enforcement agencies are enjoined to promote or at least not diminish.

By itself, exclusive franchising does not provide a manufacturer with unfettered flexibility in distribution.<sup>209</sup> Many products, particularly those sold at retail, require saturation marketing and hence overlapping sales territories.<sup>210</sup> On the other hand, exclusive franchising is precisely what manufacturers desire in many cases. The legality of that form of distribution should be recognized. Equally important, many of the economic, jurisprudential, and common sense principles that should govern the treatment of exclusive distribution apply with equal force to other types of vertical restraints. One might more easily arrive at an understanding of those other vertical arrangements from a prior understanding of exclusive distribution.

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209. See *GTE Sylvania Inc. v. Continental T.V., Inc.*, 537 F.2d 980, 997-98 (9th Cir. 1976), *aff'd on other grounds*, 433 U.S. 36 (1977); Bork III, *supra* note 25, at 183.

210. See Posner I, *supra* note 10, at 11-12; *Distribution Under the Sherman Act*, *supra* note 1, at 795.